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**A COMPARATIVE STUDY OF THE
LAW OF CORPORATIONS**

STUDIES IN HISTORY, ECONOMICS AND PUBLIC LAW

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A COMPARATIVE STUDY

OF THE

LAW OF CORPORATIONS

WITH PARTICULAR REFERENCE TO

THE PROTECTION OF CREDITORS AND SHAREHOLDERS

BY

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PREFACE

THIS book is intended as an humble contribution to the work of legislative research now being conducted at Columbia University under the auspices of the Legislative Drafting Association. I am deeply indebted to Professor Munroe Smith for much valuable assistance and for his stimulating guidance and encouragement.

A. K. K.

NEW YORK, MAY, 1912.

267]

CONTENTS

	PAGE
PREFACE	5
LIST OF AUTHORITIES	9
INTRODUCTION	13

CHAPTER I

GROUP FORMS AND CORPORATE TYPES IN ANCIENT TIMES	17
--	----

CHAPTER II

GROUP FORMS AND CORPORATE TYPES IN THE MIDDLE AGES	30
--	----

CHAPTER III

THE ORIGIN AND DEVELOPMENT OF CORPORATIONS IN ENGLAND.	43
--	----

CHAPTER IV

PROTECTION OF CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE	
—ORGANIZATION	56
1. France	56
2. Germany	65
3. Italy	85
4. Spain	90
5. Switzerland	93

CHAPTER V

LEGISLATION AND REFORM IN ENGLAND AND AMERICA—ORGANIZATION.	97
---	----

CHAPTER VI

PROTECTION OF CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE	
—OPERATION.	116
1. France	116
2. Germany	122
3. Italy	134
4. Spain.	139
5. Switzerland	140

CHAPTER VII

PAGE

LEGISLATION AND REFORM IN ENGLAND AND AMERICA—OPERATION . . . 144

CHAPTER VIII

PROTECTION OF CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE

—DISSOLUTION	155
1. France	155
2. Germany	157
3. Italy	160
4. Spain	163
5. Switzerland	164

CHAPTER IX

LEGISLATION AND REFORM IN ENGLAND AND AMERICA—DISSOLUTION . . . 166

LIST OF AUTHORITIES

- Baldwin, S. E., "American Business Corporations before 1789." *Annual Report of American Historical Association*, 1902.
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INTRODUCTION

CORPORATIONS as agencies of combination and monopoly have long been the subject of governmental regulation. Indeed, in late years, the so-called "anti-trust" problem has absorbed the attention of statesmen and publicists, somewhat to the neglect of the organic functioning of the corporation itself. Yet this is of equal importance to the welfare of the state. Burgess emphasizes that a just regulation of the internal affairs of corporations in order to afford protection to the various parties in interest is essential to sound political science. "If government does not exercise such powers and discharge such duties, it is easy to see how, through the device of the corporate organization, the few may despoil the many, and thus weaken the basis of popular government, if not of all forms of government."¹

The heterogeneous character of our state laws and the absence of federal legislation on the subject, make a comparative study of foreign legislation in conjunction with our own, both profitable and enlightening. But as each country has its own type of corporation, often existing nowhere else, it is important to limit the scope of research to a category common to all.

We propose to confine our investigations to those groups of individuals, organized for profit, recognized by the state as legal entities and having a capital divided into shares, the

¹ "Private Corporations from the Point of View of Political Science," in *Political Science Quarterly*, 1908, vol. xiii, p. 205.

holders of which are liable to an amount limited to, or measured by, the capital contributed.

A maze of definitions and abstract concepts has grown up about the legal nature of corporations and of group-forms generally. Many of these have been drawn from prepossessions in respect to the nature of some particular group-form, or class of group-forms. Definitions do not necessarily give definite impressions. Frequently they obscure those concepts which may be developed more naturally from an examination of actual types.

Theorists are frequently engaged in determining whether the entity involved in the concept of the corporation has any real existence, or exists only by dogmatic fiction. If it exist by fiction of the law only, the corporation can have no real or "collective" will, to use Gierke's phrase,¹ separate from that of the individuals composing the corporate membership. The inquiry has given rise to seemingly endless discussion, to add to which would do as little toward solving the problem of establishing a just relationship between the group and the natural individuals who enter into relations with it, as did the casuistry of the Middle Ages for the establishment of proper standards of righteous action between man and man.²

Professor Gray well points out that there is no differ-

¹ Gierke, *Die Genossenschaftstheorie und die deutsche Rechtsprechung*, p. 637.

² Freund, *The Legal Nature of Corporations*, p. 14: "Amidst an apparently irreconcilable conflict of theories, there is yet a substantial consensus of opinion as to the practical requirements in the legal treatment of corporations. That is to say, it is generally agreed that the law should regard corporations differently from joint owners; that corporate rights and liabilities should be held apart from individual rights and liabilities of the members. It is also generally agreed that this object is best accomplished by treating the corporation, as far as possible, as a distinct person."

ence in the practical results of the one or the other theory. The actual wills by which in fact the rights of the corporation are exercised, or by which duties are enforced upon it, are in each case the wills of persons designated in accordance with the organization of the corporation and the positive law of the state. Both the nature of the duties and the persons on whose actual wills those duties are enforced are the same under either theory.¹

Nor is it of vital importance to insist upon a sharp line of demarkation between what may be designated a corporation according to modern views and what, in legal effect, should be classified under the category of another type of group-form. Classifications depend too largely upon particular legislative systems to be closely adhered to. The true subjects of historic and comparative investigation, in order to attain practical results, must be the capacities of corporate action, the methods through which it operates and the rights and liabilities of individuals resulting from it. "These are the real questions of vital importance, the decision of which will not ordinarily depend on whether or not an institution is to be called a corporation, which, indeed, is little more than a question of how far a medieval nomenclature is applicable to modern institutions."²

Each particular type of group-form which has existed from the earliest commercial periods to the present day was determined by the life of the community in which it was developed and by the particular needs of the time. No type was directly or spontaneously conceived, but each was gradually evolved from some previous form, or was referable to a precedent legal conception.

It will therefore be possible to trace the type of the mod-

¹ Gray, *Nature and Sources of the Law*, p. 53.

² Taylor, *Private Corporations*, 5th ed., sec. 63.

ern business corporation to its earliest beginnings, to note the conceptions to which it owed its origin, to observe the economic environment responsible for its development and thus to obtain a clearer and more unbiased view of its functions and mode of functioning.

CHAPTER I

GROUP-FORMS AND CORPORATE TYPES IN ANCIENT TIMES

THE concept of the corporation may be ascribed to the tendency of ancient peoples to idealize into personality groups of persons, or groups of legal rights and obligations. The association of persons into groups for the achievement of a common purpose is as old as civilization itself. Modern authorities say that the clan, or family in the larger sense, constituted the earliest form of society and the beginning of the state. Original governments, says Woodrow Wilson, "had a *corporate* existence which they regarded as inhering in their blood and as expressed in all their daily relations with each other."¹ The life of the community thus grew up round the clan or tribe, and, in dealing with other clans or tribes, the conception of a corporate or collective entity became essential.² Later, these groups confederated to form the city and clans became merged in the larger entity of state.³

The growth of the Greek city-state effected a unity of

¹ *The State*, sec. 16.

² Muirhead, *Historical Introduction to the Private Law of Rome*, p. 6, note: "Recent writers are agreed, in the main, that the *gens* was originally just the *familia* in the widest sense of that term, or aggregation of *familiae* in a narrower sense. The term 'clan' is the nearest equivalent in English, and suggests a correspondence with the Celtic and other primitive clans, and there are many analogies—for example, as regards the use of a common name and supposed descent from a common ancestor."

³ Wilson, *op. cit.*, sec. 64.

public action which had not been realized theretofore. The democratic form of government was conducive to the creation of organs composed of individuals acting in co-operation both in the name of and for the common good of the state. The state thus became idealized and its property dealt with as an aggregate.

This idea became more and more widely developed in the Roman state, as the economic transactions undertaken in its name became more complicated. The state, or *populus*, was deemed capable of entering into transactions with individuals as though it were itself an individual, with this difference, however, that it had certain rights and privileges which individuals did not enjoy. The sovereignty inherent in the state made it the source of all rights. Hence disputes growing out of transactions between the state and an individual were not cognizable by the ordinary courts, but were submitted to the administrative judgment of the censor.¹ So, too, the rule of the inadmissibility of direct representation, characteristic of the Roman system of individual relations, was inapplicable to the state, for the acts of the state were necessarily those of its officials. It could not act except through them.

The state was originally the only juristic entity with full power to hold property directly. The old private law of Rome was conceived for the individual citizen alone and individual property was the only property recognized. The property which was designed for the special purposes of certain groups (*collegia*, *sodalitates*) had to be formally vested in one or more individual members, and treated as though it were his or their separate property.²

Sohm says that to affirm the existence of juristic per-

¹ Mitteis, *Römisches Privatrecht bis auf die Zeit Diokletians*, i, p. 348.

² Sohml-Ledlie, *The Institutes*, sec. 37.

sons is to affirm the existence of a particular kind of property, *social* property, or property appropriated to the purposes of a particular society or community.¹ Accordingly, Roman law treated state property as social or public property (*res publicae*), ancillary to the purposes for which the state itself existed and not subject to the rules of ordinary proprietary transactions (*extra commercium*).

The intimate affairs of the town communities, however, were necessarily conducted in a manner more nearly approaching private transactions. The simile so often employed to-day between municipal government and private business held good in early periods as well. The *municipium* thus appeared to be the first to rank in law with the *cives*, capable of private rights and duties.²

Later, the treasury of the state, or *fiscus*, also became segregated into an aggregate of rights and obligations, separate and apart from its actual property. This also was invested with an ideal or juristic personality, by a system of reasoning which Savigny has designated as a "sort of artificial reflection drawn from within."³

When we recall that the government of the early Graeco-Roman period was centered in the city, it is clear how easily the idealization of the popular will represented in the state came to be applied, though in modified form, to the municipalities as well, even after they had lost their complete autonomy. The government of Italy, from the beginning of Roman supremacy, centered about a large number of provincial towns. These originally constituted independent states and when brought under subjection were still treated, in a measure, as autonomous communities.

¹ Sohm-Ledlie, *The Institutes*, sec. 37.

² *Ibid.*, sec. 37, p. 199.

³ *System des heutigen römischen Rechts*, bk. ii, sec. 87.

They thus retained their character of juristic entities, with this modification, however, that, being dependent upon Rome, they were subjected to the law and under the jurisdiction of the civil courts.

It is not surprising to find a well developed corporate theory of the town in the Republican period, for the aggregate group-form was typical even of the primitive community. There is much to be said in favor of the belief that at one period all property rights were traceable to the community, or at least "to larger societies composed on the patriarchal model."¹ The internal arrangement of the group was a matter of prime importance; the relation of the individual to the group became a fixed status, which (in certain communities at least) might be sold like a share of stock, the purchaser succeeding to the liabilities which the vendor had incurred toward the aggregate group.² In this manner, the community departed from its original character as a union of kinsmen and became a group of individuals, only nominally united by blood, but in fact united by their common interest in an undivided state of property.³

Later, the legal separation of persons constituting members of the community from the concept of the community

¹ Maine, *Ancient Law*, chap. 8, p. 260. There seems to be a difference of opinion as to the precise period wherein the concept of juristic personality arose. Maine seems to think that it existed in some form in very early communities, whereas Sohm is of the opinion that it was "the product of a very advanced age of legal development." Sohm-Ledlie, *The Institutes*, sec. 37.

² Maine, *op. cit.*, p. 257.

³ *Ibid.*, p. 256. "No institution of the primitive world is likely to have been preserved to our day, unless it has acquired an elasticity foreign to its original nature through some vivifying legal fiction. The village community then is not necessarily an assemblage of blood relations, but it is *either* such an assemblage *or* a body of co-proprietors formed on the model of an association of kinsmen."

as a whole approached completeness. Even the sum of its members could not, by their joint acts, bind the whole, unless the act could be said to have been that of its official organs.¹

The logical reasoning of the Roman jurists carried the idea of separate entity to conclusions from which modern law has gradually drawn away. The community was strictly an impersonal subject of rights and an impersonal object of duties. It could not be held to liabilities resulting from guilty intent, because an artificially created entity could not, under Roman principles, be capable of guilt, much less of evil intent. A municipal community could therefore not be held liable in tort by the *actio doli*, though the individual officials (*e. g.* decurions) might be personally liable even though they had acted in the name of the community.² In the very book in which Ulpian expounds the entity idea in respect of public corporations, excluding them from a possible liability for fraud, he asserts a right of action directly against the official, irrespective of the fact that the nominal defendant might be a *populus*, *curia*, *collegium*, or *corpus*.³ If the community had been enriched, it was compelled, of course to restore that which it had unlawfully received.⁴

We have observed that the organized bodies of society, the state and the municipality, were conceived in the light of separate economic establishments for convenience in a larger sense; in other words, that they might more com-

¹ Mitteis, *Römisches Privatrecht*, sec. 18, p. 341.

² Savigny, *System*, bk. ii, chap. ii, sec. 95, citing *Dig.*, iv, 3, 15, sec. 1.

³ *Dig.*, iv, 2, 9, § 1. A law of Majorian forbids judgment to be taken against a *curia* as an entity; it may only be taken against its guilty individual members. *Nov. Maj. Tit.*, 7, cited in Savigny, *op. cit.*, sec. 95.

⁴ Savigny, *op. cit.*, bk. ii, ch. ii, sec. 95, citing *Dig.*, iv, 3, 15, sec. 1.

pletely fulfill their functions. "It was to enable the community as a whole to take part in the economic life of the nation on the same terms as the individual."¹ With this development, other forms of social property made their appearance, to which the peculiar nature of the pagan religion was conducive. In a system requiring numerous temples, each under the temporal control of different bodies or colleges of priests, the segregation of proprietary rights was inevitable.²

A further consolidation of property rights resulted from the peculiar method which the Roman state had adopted, similar to Greek and probably also Egyptian practise, in the collection of its ordinary revenues.³ The state did not act directly in the collection of its taxes; until comparatively late in the Imperial period, it farmed them out, by various franchises, according to locality and the nature of the tax.⁴ This franchise continued only for a fixed period, usually for a year. Although the historical data are incomplete, it seems that the importance of the undertaking and the degree of responsibility demanded from those who applied for the franchise made some form of combination essential. But as the state always insisted upon dealing with a single individual, probably for the sake of

¹ Sohm-Ledlie, *op. cit.*, sec. 37, p. 205 note.

² As an illustration of the extent to which this segregation proceeded, it is interesting to recall that as late as the early Roman Empire, a legacy to the temple of Diana was a legacy to *Diana*; and to escape the incapacity of celibacy introduced by the *Lex Papia et Poppaea*, Diana had to receive formally the *jus liberorum*. Ihering, *Scherz und Ernst in der Jurisprudenz* (4th ed.), p. 113.

³ For the origin and early development of this institution among the Greeks and Egyptians, see Böckh-Fraenkel, *Die Staatshaushaltung der Athener*; Lumbroso, *Recherches sur l'economie politique de l'Egypte sous les Lagides*, cited Lehmann, *op. cit.*, p. 6 note.

⁴ Kniep, *Societas publicanorum*, p. 90.

simplicity and a greater concentration of responsibility, the group formation was employed only in the execution of the enterprise and the division of the profit (or loss). It did not function in transactions with the state itself.

The chief publican, or *manceps* (sometimes called *auctor emptionis*) thus organized his enterprise into a joint association (*societas publicanorum*) for the purpose of raising capital in sufficiently large amount to guarantee his success in bidding for the franchise. For the capital advanced, his associate capitalists became partners (*socii*, μετέχοντες) according to agreement.¹ The Roman state recognized the *manceps* alone, not the partners who had furnished the whole or a part of the capital, though it doubtless had notice of their existence by a system of registration. If one of the partners was guilty of a wrong in the exercise of the delegated function of gathering the taxes, all of the partners were equally liable and there was no restriction of liability to the amount of the capital contributed.² The relations *inter se* differed from that of the usual partnership in certain elements tending to weaken the importance of personality, though by no means entirely eliminating it. The liability of the partners was not limited except *inter se*, pursuant to their agreement with the *manceps*, but the capital, even though a fixed sum, probably did not consist of assignable shares. The death of one of the partners did not effect a termination of the relation, provided it were originally agreed that the heir might be substituted in place of the deceased. Even if there were no precedent agreement, the substitution might be made if the heir was not personally unacceptable to the survivors.³ Differing from

¹ Kniep, *Societas publicanorum*, p. 240; Lehmann, *Das Recht der Aktiengesellschaften*, i, p. 6.

² *Dig.*, xxxix, 4, 6.

³ Lehmann, *op. cit.*, p. 15.

the customary partnership, the fund was deemed a permanent one, without right of division until the completion of the enterprise.¹ Thus if the heir was not admitted, he had no right to an immediate accounting but was compelled to take his chances with the enterprise until the termination of the franchise period.²

We see a tendency then, even in this primitive form of association, to provide a method of succeeding to the relations of the member to the group, without disturbing the continuity of function of the group itself. The development of the Roman law of private property was essentially utilitarian and variations from its established rules were usually made only after long periods of contrary practise. "Originally, it was neither capable nor desirous of supplying the law for any other proprietary relations but those of private persons in the strictest sense of the term, *i. e.* individual persons."³ The demands of these huge aggregations of private capital for the purpose of farming the revenues, however, gradually introduced variations from the partnership form of association; but these did not go beyond the necessity of each case. There was no need for a corporate name, because the *maniceps* was the responsible head of the organization and the contractual relations of the state existed only with him.

The law of Rome, both in the late Republican period and in the Empire, recognized no freedom of association and was opposed to all societies on principle.⁴ Authorized pri-

¹ Kniep, *op. cit.*, p. 254; Lehmann, *op. cit.*, p. 14. Like municipal communities, the *societas publicanorum* enjoyed the right of direct representation through a *syndicus*, or *actor*, denied, in the Roman system generally, to private individuals. Kniep, p. 250.

² Lehmann, i, p. 14, citing *Dig.*, xvii, 2, 59, and *Dig.*, xvii, 2, 63, § 8.

³ Sohm-Ledlie, *The Institutes*, p. 201.

⁴ Mommsen, *Staatsrecht*, vol. ii, pp. 886 *et seq.*

vate societies were compared to the corporations of public law—*ad exemplum reipublicae*¹—and permitted to hold property like municipal communities. This applied to the benefit and burial clubs as well as to the numerous associations (*collegia*) of tradesmen and artisans, membership in which, though originally voluntary, had become compulsory in the fourth century. They had their own regulations and officers; also a capital fund from which the income was distributed (*emolumentum*) but from the body of which (*arca*) nothing could be taken.²

All public corporations were *ipso facto* recognized in law under the Empire and their legal personality followed as an incident.³

The idea of the separate entity of the group was essentially a development for the convenience of social order within a community. The requirements of the *municipium* and of the peculiar form of local government which was prevalent toward the end of the Republic, demanded a segregation of the property of the community from that greater aggregate of public property which belonged to the dominant Roman state as a whole. The gradual identification of certain public property with the community to the use of which the particular property was subservient, created a set of rights and duties of the local government with relation to that property. The entity idea was thus developed as one of the instrumentalities of government

¹ Sohm-Ledlie, pp. 202-4, 209, citing *Dig.*, iii, 4, 1, sec. 1. Thus a *societas publicanorum* [*rectigalium publicanorum socii*] might be confirmed in its corporate existence by senatorial decree. Kniep, *op. cit.*, p. 241.

² Brown, "State Control of Industry in the Fourth Century," in *Pol. Sci. Quar.*, ii, p. 494; Liebenam, *Zur Geschichte und Organisation des römischen Vereinswesens* (1890), *passim*.

³ Sohm-Ledlie, *op. cit.*, p. 209.

and as a more convenient juristic method for rendering precise the respective rights and duties existing between the community and the individual. The Empire saw its adoption into settled law. It was not consciously evolved in order to create new subjects capable of private ownership.

Writers often fail to emphasize this distinguishing feature of the Roman concept of the corporation. Some have even ventured the assertion that "the Roman corporation was much the same as the corporation of modern times."¹ If the statement had been restricted to municipal and quasi-public corporations, it would have been more easily defensible. In regard to these, it may be said that the emphasis which the Roman law placed upon individual rights as opposed to the communism of the Teuton tribes, was the very force which so completely developed the entity idea. The property of the corporation became collective property, not only distinct from that of its members, but property in which the members had no direct ownership, divided or undivided. Their interests were *in personam* the corporation itself. Under the Roman development of group-forms, "the rights and liabilities of a corporation were not the rights and liabilities of the sum total of its individual members, but exclusively the rights and liabilities of the collective whole of its members, that is, of the corporation as such."²

The entity idea has too often been held responsible for the origin and growth of incidents of the group-form of private enterprise which really are not at all necessary, nor historically referable thereto. Chief among these incidents of the modern group-form is the exemption or limitation

¹ Cook, *On Corporations* (6th ed.), p. 4, sec. 1.

² Sohm-Ledlie, *op. cit.*, p. 200.

of the liability of the members for acts of the group. The separation of personality results in a capacity to have separate rights and to protect them by legal action (*ester en justice*); to have separate duties and to be subjected separately to the remedial procedure of the law. It does not necessarily or logically follow that the members should be absolved from responsibility for the acts of the group-personality. The will of the group-personality represents the collective will of the members composing the group. It makes no difference whether we accept one or the other theory of the group-personality under the dispute already alluded to. It is immaterial whether we follow the opinion of civilians, such as Ihering¹ and Windscheid,² who contend that the sole subjects of group rights are the members and that the personality is fictitious, or the view of the Germanists, as represented in the writings of Gierke³ and Zitelmann,⁴ that the personality is real. In either event, the members have chosen to merge their wills into the collective will of the group. Collectively they have constituted the constitutional organ of the group as a mandatarly implied in law to act in their behalf.⁵

It is often urged that even in the Roman law this ex-

¹ *Geist des römischen Rechts*, vol. 3, p. 343.

² *Pandekten*, vol. i, sec. 49, p. 122; sec. 57, p. 139.

³ *Die Genossenschaftstheorie*, p. 5 *et seq.* See also Stammer, *Theorie der Rechtswissenschaft* (1911), p. 356.

⁴ *Begriff und Wesen der sog. juristischen Person*, sec. 13, p. 53.

⁵ Davis, *Corporations, their Origin and Development*, p. 25, says: "The fact that the common group-will may not coincide completely with the will of any one member ought not to exempt the members from responsibility for the effects of its execution." Klingmüller, *Die Haftung für die Vereinsorgane*, in Leonhard's *Studien zur Erläuterung des bürgerlichen Rechts*, 1900, pp. 22-23, inclines to the Romanistic view. He refers the capacity of the corporation to act and to be made responsible for its acts to the will of the legislator.

emption was recognized. If anything is owed to the group, it is not owed to the members individually; nor do they owe what it owes. *Si quid universitati debetur, singulis non debetur, nec quod debet universitas singuli debent*.¹ This passage is often relied upon to prove that the Romans had already recognized a limited liability as incidental to the group-form.² We have observed that this was applicable only to public corporations and to those beneficial groups, usually of pious or eleemosynary character, assimilated to that class by a *lex specialis*.³ Even in this class, the relation of the group to its members empowered it to compel them to contribute sufficient funds to enable it to meet its obligations.⁴ A number of writers have pointed out that there was no need for a commercial device with limited liability because trade was conducted by the slaves and the Roman law of *peculium* permitted the master to participate in profits without risking more than the capital embarked in the enterprise.⁵

We have seen then that group-forms, as the subjects of legal rights and the objects of legal obligations, had their origin in the functioning of governmental authority in early communities. The economic needs of the clan or tribe,

¹ *Dig.*, iii, 4, 7, § 1.

² See for example Taylor, *op. cit.*, p. 2; Davis, *op. cit.*, i, p. 26; ii, p. 221.

³ See Sohm-Ledlie, pp. 209-210, citing *Dig.*, iii, 4, 1, and *Dig.*, xxxiv, 5, 20.

⁴ Savigny, *System des heutigen römischen Rechts*, bk. ii, chap. ii, sec. 92.

⁵ Renaud, *Das Recht der Aktiengesellschaft*, p. 8; Fick, "Ueber Begriff und Geschichte der Aktiengesellschaften," in *Zeitschrift für das gesamte Handelsrecht*, v, pp. 1, 31; Deitzel, *ibid.*, ii, pp. 1, 10. See also Buckland, *The Roman Law of Slavery*, p. 233. It must be remembered, however, that the liability of the master was much extended by the praetorian *actiones exercitoria, institutoria, and quasi institutoria*. *Ibid.*, pp. 169, 174.

and later, of the city-state, demanded a segregation of property which gradually led to a segregation of the rights and obligations with reference to that property. In no sense did the group-form originate in the necessities of private commercial initiative: it was developed from the agencies called into existence for the more convenient exercise of the political and religious functions of the state. The consolidation of municipal and sacral property and rights was followed by consolidations of property and rights of the state as a whole, in the exercise of specific functions.

The consolidation of the rights and obligations of groups of private individuals with a separate legal entity was recognized only in conjunction with the exercise of public functions, though these, it is true, became interpreted in a somewhat extended sense. But the entity was co-extensive only with the public purpose which it subserved. Even the group form most nearly approaching the modern corporation, though a result of private enterprise and subservient to private interests, was permitted because it was, at the time, the most convenient method of collecting *state* revenues. It bore the character of an economic, rather than a legal entity. Persons alone were the subjects of rights under Roman law. The right of association was denied for reasons of public policy. Even Gaius does not mention legal or juristic persons in his classification.¹ He recognizes their existence for specific purposes merely. The great significance of the Roman period lies in the fact that the forms which had developed in satisfying the *economic* needs of *state* action and which were tolerated, though not recognized in law, were found readily adaptable to the operations of *private* initiative in later periods when, under greatly varied forms, they became crystallized into complete legal entities.

¹ Dig., xlv, 1 22; "*personae vice fungitur*."

CHAPTER II

GROUP-FORMS AND CORPORATE TYPES IN THE MIDDLE AGES

THE growth of association types was stimulated by the encouragement given to corporate organizations by the church. The independence of the Roman temples, supplying the motive for separate entity during the pagan period, was now supplanted by the independence of monastic establishments, each leading a life complete in itself within the walls of the cloister. The internal regulation of the monastery as decreed by St. Benedict in 529 gave organization and permanence to the corporate idea. Each monastery was a unit and the property of all of its members was held in common.¹ Even the church itself was incapable of absorbing them. "As often happens in the development of corporate life, the superior organization of society proved unable to absorb into its own structure the inferior corporate life it had called into being; it had to be content with annexing the subordinate structure."² Indeed, with the spread of the monastic principle, the church organization itself disintegrated into corporate units, so that cathedral and collegiate chapters also became subject to the canon rule of common life.

The canon law developed co-extensively with the influence of the church. It constituted, as it were, an advance guard of that later invasion of Roman jurisprudence which

¹ Davis, *op. cit.*, pp. 50-51.

² *Ibid.*, p. 56.

culminated in the peaceful conquest known as the "Reception." The church applied the Roman law in its own courts, modified in accordance with ecclesiastical conscience, long before the acceptance of the Justinian law books in the secular courts.¹ Accordingly, the corporate organizations of the church and the charitable entities developed from the *piae causae* of the Roman system were well recognized by European society before the final period of the reception in the sixteenth century had been reached. The Roman conceptions of legal entity were thus readily applied to secular institutions. Vinogradoff says that the reception (in France) did "not start with the acceptance of an external authority from which all changes in detail should be derived, but from a kind of struggle for existence between the concrete rules and institutions of German and of Roman origin."²

The destruction of Rome and the infusion into European society of unorganized Germanic elements called into existence a number of group types which served the immediate social and economic demands of the times. These must not be regarded as prototypes of corporate organization in the modern sense, for they neither possessed a common fund nor were they devoted to a definite enterprise for profit. To this class belong the guilds and other industrial societies, the objects of which were general welfare, regulation of prices, monopolization of particular vocations and the like. They were not antecedent corporate types, but developed concurrently. Sometimes, devices for the participation of profits formed part of the group-plan, and thus their experience influenced the development of more distinctly corporate types. On the Continent, as in Eng-

¹ Sohm-Ledlie, *op. cit.*, pp. 143-144.

² *Roman Law in Medieval Europe* (1909), p. 65.

land, the same bond of common personal interest formed the basis of membership in the union. Cultivation of the land was often carried on within definite areas by agrarian associations (*Mark-Genossenschaften*; *Real-Genossenschaften*) so as to control production and consumption in the interest of the community.

At times, however, economic interests triumphed over social and communal considerations. This produced a type no longer identical with the guild, though but slightly approaching corporate forms. Troplong¹ recounts that, as early as the twelfth century, certain mills in southern France had been transferred to associations of "*pariers*," or equal owners. The mill was divided into shares of equal value called "*uchaux*," or "*saches*" (sacks), originally measures of capacity. These terms were probably first used to denote the approximate income of a share. The organization was managed by a syndic, a number of directors and a treasurer, elected by the *pariers* in general meeting. Troplong considers the *uchaux* equivalent to shares of stock, an opinion which he finds justifiable in view of the fact that similar mill associations exist to-day in the same part of France with shares properly so-called. But there is no evidence that, in their original form, the liability of the shareholders was limited. Similar associations existed in the neighborhood of Cologne and, as to these, Gierke has pointed out that the assignability of the *partes* was not inconsistent with a liability to pay assessments.²

An interesting stage in the development of the concept of a common capital is to be found in the operative associations (*Genwerkschaften*) of the twelfth and thirteenth

¹ *Commentaire du contrat de société*, p. xxviii, cited by Lehmann, *op. cit.*, i, p. 22.

² *Genossenschaftsrecht*, i, pp. 968-971.

centuries. Here again the primal consideration was personal. In fact, originally, the enterprise was divided into parts, of which each member undertook to operate one or more without central control and in separate ownership. The association had merely a privilege of purchase upon the withdrawal of a member, doubtless as an insurance of the personal bond to which we have drawn attention. Where co-ordinate management was essential, as in the operation of mines, the central organs undertook to engage laborers and incur expenses generally, which were met by levies (*Samkost, expensa*) on the members. In this way, the idea of separate ownership gradually disappeared in favor of ownership by the members jointly, leaving a right of participation only. With this growth of the capitalistic idea, the parts, no longer tangible, soon increased by division into smaller and smaller shares (*Kuxe*). These were measures of voting rights, of profits and of the duty to pay assessments; as a result, they came to have a variable value per unit. In case of transfer of the shares, all further levies went against the new owner, but those already matured were personal obligations, to be met on pain of forfeiture of the share in favor of the association, or in favor of the person who had advanced the assessment.¹

One would have surmised that a type so closely resembling a corporation in many of its outward features would have advanced to the final stage of participation, conceived as a chose in action or movable property right. This was never realized, doubtless because the enterprise was restricted to a definite physical object; so that it was not impossible to conceive of a small undivided right in the particular property which constituted its capital.

¹ Opet, "Das Gewerkschaftsrecht nach den deutschen Bergrechtsquellen des Mittelalters," in *Zeitschrift für Bergrecht*, vol. 34; cited in Lehmann, *op. cit.*, pp. 24-25.

The mill and mine operators' associations were devices largely, if not primarily, designed to limit the liability of members to the capital embarked. They were probably among the earliest instances of aggregations working upon this plan, a result to which the disappearance of slavery may have contributed. On the other hand, personal qualification was still the basis of membership and there were no external legal guarantees for the protection of the interests of the individual member as against the union. Indeed, these incidents were closely related; for membership was the result of connection with the craft, so that the members had full knowledge of, if not actual participation in, the enterprise itself.

It cannot be said that either of these was the immediate forerunner of clearly corporate types. Indeed, the chain of development was not at all continuous. Early corporations were the results of many antecedent trade devices developing concurrently in accordance with the particular group-form which each occupation or trade tended to assume.

The maritime partnership of this period (*societas navalis*) presents an example of a near-corporate organization. The ship itself constituted the capital, divided into *partes* owned by *partitionarii*. The parts or shares were assignable, but often subject to a privilege or option of first purchase by the *co-partitionarii*. Routine matters were determined by the majority, and liability was limited as against third parties to the interest of the partners in the ship (" *tot ho paga la nau* "). Assessments could be levied against the various owners of the *partes*, but any owner could escape further liability by abandoning his interest.¹

A most interesting development from these maritime as-

¹ Goldschmidt, *Universalgeschichte des Handelsrecht* (1891), p. 340; Lehmann, *op. cit.*, i, p. 28.

sociations was the *colonna*, the organization of which is described by the tables of Amalfi.¹ The *colonna* originally represented a maritime association in which the crew (*nautae*) were also partners. In the group-form of the Amalfi tables, these two classes united with a third, the members of which contributed capital in wares and money—so that the shipowners, crew, and contributors all became interested in the entire enterprise (*una massa et unum corpus*) and received a new general designation, “*compagni*,” later, “*colonnisti*.”

Renaud sees in this a combination of the usual maritime association with the *commenda*. This was a form of undisclosed agency by which the agent, entrusted with money or wares for speculation by one or many principals (*commendatores*), was alone responsible as against third parties. Both institutions suffered a change, for the contributors of the wares or money presently became active members of the *colonna*, had a voice in its management, shared proportionately in the profits of the whole and were responsible for the losses to the extent of their contribution. The captain was the leader of the enterprise. The members enjoyed a certain protection through his obligation to make public the amount of the entire capital contributed and the purposes of the voyage.² For all liabilities undertaken by the captain the creditors had recourse to all the assets of the *colonna*, as well as to the private fortune of the captain, but not to that of the other *compagni*.³ The captain was subject to the directions of a majority of the

¹ Renaud, *Das Recht der Actiengesellschaft*, p. 13. See the authorities cited in note on p. 12 as to the origin and nature of the institution.

² Renaud, *op. cit.*, pp. 13-17.

³ *Ibid.* See also article by Laband, “Das Seerecht von Amalfi,” in *Zeitschrift für das gesamte Handelsrecht*, vii, p. 314.

crew, or of the members of the *colonna* as such.¹ After each cruise, the members were entitled to an accounting from the captain, and the profits were divided among the various classes of the members, a definite proportion going to the captain, the crew and the owners of the ship respectively, the balance to the *commendatores*.²

A further approach to corporate formation is visible in the instrumentalities called forth by the Italian states in their indirect methods of tax gathering. We have already pointed out that the Roman *societates publicanorum*, though not continuing in their ancient character beyond the Roman period, yet exerted an influence upon later group-forms created for similar objects. As early as the twelfth and thirteenth centuries, public loans were made upon the credit of specified taxes, such as those upon wine and salt. The entire loan (*mons, massa, maona, or compera*) was divided into equal parts (*loca, luoghi, or partes*) of a definite par value and entered in a public register (*cartulario*) with the name of the holder of each part.³ The parts were assignable and inheritable. The nature of the security required a joint management, to accomplish which the owners of the parts organized associations (*societates comperarum*) for their protection and advantage. These gradually developed into enterprises for profit, apart from the purpose of securing the return of interest and principal. Examples are to be found in the Genoese *Maona* of Chios and Phoea (sometimes designated as the *Maona* of the Giustiniani, 1346-1566) and that of Cyprus (1373-1408) both of which were organized as huge colonial

¹ *Tabula de Amalfi*, art. 7, "*omnium nautarum vel sociorum saltem majoris partis*." Laband in *Zeitschrift für das ges. Handelsrecht*, vii, p. 317, note 53.

² Renaud, *op. cit.*, pp. 15-16.

³ Goldschmidt, *Universalgeschichte des Handelsrechts* (1891), p. 292.

companies. The enterprise as a whole was directed by officers (*protettori*) elected by the shareholders and under the orders of a general assembly and those of a smaller body, or council.¹

The nature of these organizations may be best observed in the operation of the *monte* or *società delle compere e de' banchi di S. Giorgio*, or Bank of St. George, in which the system attained its highest development. This great institution was founded in 1497 as a result of the consolidation into one great fund of the numerous *comperae* of the two preceding centuries. It continued down to the fall of Genoa as a free state, in 1816.

At first, the old form of loan upon interest with security was adopted, but in 1418, instead of the usual high rate of interest (eight per cent), it was provided that the holders should be entitled merely to dividends (*provento utile*) according to the profits of the many activities and privileges enjoyed by the bank under its charter. The *luoghi*, or shares, were of the par value of 100 lire each, registered and transferable, and certificates were delivered when required. Generally, however, the evidence of ownership was the public register.

The organization of the Bank of St. George gives clear evidence of the fact that the early principle of corporate management was based upon control by the large shareholders. Those owning less than ten *luoghi* were deprived of a vote in the general assembly. The eight *protettori* were in turn elected by the largest shareholders of the general assembly. The *protettori* as well as the *procuratori* and *syndicatori* were obliged to hold a large number of shares.²

¹ Goldschmidt, *op. cit.*, pp. 295-296.

² *Ibid.*, pp. 297-298.

In express reliance upon the type of the Bank of St. George, a plan for refunding the debt of the city of Milan was proposed to the authorities by one Zerbi, at the end of the sixteenth century. Though the plan was originally accepted as a method for conducting the city's own finances, it soon became operative as a separate bank under the name of the Bank of St. Ambrosius (1598). The type was essentially different from that of the Genoese institution; for, though we again have *luoghi* with a par value, assignable and evidenced by a certificate (*cartella*), yet there was no voice on the part of the holders in the management of the enterprise. The contributions were made to the bank and not directly to the state, as in the earlier type. Furthermore, the *luoghi* were repayable after certain periods and were not continuing obligations, without a date of maturity. The holders were not responsible for the obligations of the bank, and being entirely excluded from a voice in its management, must be deemed to have been limited partners rather than members of a corporate group-form.¹

It is at this point that a continuity of juristic development seems to fail. The Bank of St. George, with the single exception mentioned, found no successors in history. Banks continued to be conducted by private individuals, without corporate existence, until the constitution of the Bank of England, in 1694. Perhaps the organizations produced by the peculiar financing of the Italian city-state of the fifteenth and sixteenth centuries were unsuitable elsewhere. From this time the corporate form progressed among ship-owners and merchants engaged in colonial exploitation. In this movement, practically every country in Europe bordering on the western and northern sea coasts participated. Very different, however, was the organiza-

¹ Lehmann, *op. cit.*, pp. 46-50.

tion of all the commercial group-forms by which these enterprises were undertaken, from the financial group forms in Italy during the period immediately preceding.

The type of practically all the Continental maritime companies was set by the Dutch East India Company. Its charter was granted in 1602 as a consolidation of eight smaller "companies" whose organization, like that customary in the Low Countries at the time, was that of partnership, with a liability limited sometimes expressly by charterparty, sometimes by custom, to the value of the ship and freight.¹ The right of each shareholder now lay, not in a claim for principal advanced to the state, as in the case of the Bank of St. George, or contributed for a period to the organization itself, as in the case of the St. Ambrosius Bank, but in a right against the company to receive dividends. The Italian types represented simply a collection of creditors compelled to take on certain corporate characteristics to preserve their principal by ensuring its gradual amortization through profits. The Dutch East India Company received its grant of monopolies by charter and, incidentally therewith, its separate juristic existence as a body corporate and its rules of operation. The fact that its members were free from liability to third parties resulted from the nature of the *enterprise*, not from the nature of the *organization*.

Following the example of this company in the Netherlands, the Dutch West India Company was chartered in 1621; in Denmark, the Danish East India Company, in 1616; in Sweden, numerous commercial companies, from 1615 onwards; in Portugal, the East India Company, in

¹ Voet, *Comm. ad xvii*, 2, no. 15: *idque propter rationes easdem, ob quas usu obtinuit, exercitores liberari ob obligatione ex magistri contractu nata, si partes suas quas in navi habent, derelinquere parati sint.* Lehmann, *op. cit.* i, pp. 56-67.

1628; in France, the two great India companies, in 1664.¹ As a result of the political and public nature of these organizations and of the peculiar functions which they were expected to perform, the state exercised a more or less extensive control. Thus, sometimes a part, sometimes the whole personnel of management was appointed by the state; the regulatory acts or by-laws were also subject to its control. Furthermore, both creditor and shareholder possessed a guaranty of fair treatment in that the state supervised, not only through its appointees among the managers, but also directly, the accounts of the organization and the apportionment of dividends.

The clear establishment of a *right of action* for an accounting and for dividends, if any, and for the return of the investment only after a definite period, as opposed to a property right in the capital of the organization itself, is distinctive of this period and is originally referable to the Netherlands, rather than to England. We shall see that, in the early seventeenth century, the right of the stockholder was there limited to the profits of a particular voyage or series of voyages. While this tended to impede the juristic development of the idea in England, the Dutch type, wherein the interests were continuous, at least for a definite time, though the accountings were periodic, permitted its rapid growth in practice. It is to the Dutch then that we owe the term for share, "*Aktie*" (French, "*action*;" German, "*Aktie*;" Italian, "*azione*;" Spanish, "*accione*").

In these companies, the capital was not originally divided into equal parts, as in the Italian banks. A minimal statutory contribution was provided for, but gradually the equal-share idea came into practice and also a definite capital or "*fond perpétuel*." At first the dividends were paid out, without reserve, after each voyage. Later,

¹ Lehmann, *op. cit.*, i, pp. 59-60.

with the development of a definite share capital, periodic dividends, mostly yearly, were provided for, and also the maintenance and accumulation of reserve funds for the equalization of dividends.¹ The Dutch type represented a clear departure from the precedent craft associations, in that the shareholder acquired no right in the capital, or other property of the organization as such. Creditors of the individual shareholder could therefore execute their demands, not against any part of the corporate capital, but only against their debtor's right to demand his quota in liquidation.

The Dutch East India Company dealt with its shareholders through subordinate chambers located in each of the Dutch provinces. It accepted subscriptions in the name of the Company and distributed the dividends. The ventures, however, were under the separate management of the chambers, while the division of profit and loss was under the control of the central governing body, which distributed dividends to the chambers in proportion to their respective contributions to the general fund (*generale Masse*) and these, in turn, to the individual shareholders after the separate expenses of the chamber had been provided for.²

We are dealing with the period of ambitious commercial expansion. The program of most of these organizations demanded, at the outset, a huge capital as the sinews of exploitation. This, perhaps more than anything else, caused the democratization of corporate types by a process similar to that progressing in England at about the same period.³ Subscriptions were invited by an offer (*Angebot*)

¹ Lehmann, *op. cit.*, pp. 63-64.

² Lehmann, *Die geschichtliche Entwicklung des Aktienrechts bis zum Code de commerce* (1895), p. 34.

³ See *infra*, ch. iii.

to the public generally, and were payable in instalments. We have seen that, originally, the evidence of participation was to be found in the books of entry. The practice of delivering an abstract of such entries led to the issue of a receipt upon the payment of the first instalment, constituting a more convenient and public evidence of participation (*billet d'action*, *Aktie-Brief*, *Obligation*, *Lott-Sedel*).¹ Frequently, payment of all the instalments became a condition of the negotiability of a share. This resembles certain provisions in modern statutes protective of stockholders and creditors.² At first there was no special form of assignment; later, entry of the assignment in the books of the company was required; finally, the memorandum of transfer was placed upon the certificate itself. In the seventeenth century, therefore, certificates of stock were registered and issued in the name of the owner. Not until the eighteenth century were certificates issued to bearer, a method accomplishing transfer by delivery and dispensing with entry in the books of the company. This type of stock, with its accompaniment of dividend coupons attached to the certificate, is the one most favored in practice at the present day upon the Continent of Europe; it is quite neglected in England and the United States, where the older system of registered stock has been almost universally adopted in practice.

¹ Lehmann, *op. cit.*, p. 65.

² See *post*, ch. iv, subdiv. 1; ch. iv, subdiv. 2.

CHAPTER III

ORIGIN AND DEVELOPMENT OF CORPORATIONS IN ENGLAND

IN England, as in ancient Rome, the origin of the corporate idea is to be traced to the municipality.¹ Long before the juridical conception of an artificial civic body came into being, the borough had what may be called a *natural* corporate existence. It was an aggregate body, acting as a unit, making by-laws, having a common seal, holding property in succession, and appearing in courts of law.²

Side by side with the community of the town, another community existed, possessing commercial privileges and representing the nucleus of town government as delegated by charter from the king. This was the Guild Merchant, or *gilda mercatoria*, which seems to have derived its origin from Norman custom.² It represented an aggregate of privileges, chief of which was the monopoly of merchandising. But the existence of a Guild Merchant in a town or borough was distinct from that of its corporate entity, or *communitas*, and must not be identified with it. The Guild Merchant was simply an instrument of town government.³ Though Coke was of the opinion that the granting of the Guild Merchant was identical with incorporation,

¹ Davis, *Corporations, their Origin and Development* (1905), ii, p. 217.

² Gross, *The Gild Merchant* (1890), i, 95.

³ *Ibid.*, p. 4.

modern authority seems to favor the view that these privileges existed separately.¹

Furthermore, the Guild Merchant is to be distinguished from the craft guilds which began to grow up as early as the reign of Henry I. It represented all traders and all crafts, while the craft guild represented the interest of a single craft. The members of these craft guilds enjoyed the monopoly of working and trading in a particular industry. With the specialization of industry they multiplied to the gradual disintegration of the old Guild Merchant.² Where the local demands could be satisfied by one general association, there was a single "company of merchants." Sometimes such a general company of merchants existed concurrently with companies restricted to a particular business. At any rate, the Guild Merchant, especially on its social and economic side, became superseded in many of its functions; so that by the sixteenth century the craft guilds and companies of merchants were the true centers of mercantile enterprise.

Besides these bodies there existed the "Company of the Staple of England," the origin of which is uncertain. Gross ascribes it to the period following the reign of Edward III. It has continued its existence down to the present day.³ The merchants of the staple had a monopoly of purchase and export. From about the reign of Edward I centers for the collection, trial, appraisal and assessment of goods, known as staples, were established in the Continental ports bordering the Channel, and afterwards in English towns as well. Their privileges were confirmed in 1353; they had their own customs and tribunals and formed in fact "a subordinate estate of the realm."⁴

¹ Gross, *op. cit.*, p. 103.

² *Ibid.*, pp. 115-117.

³ *Ibid.*, p. 145.

⁴ Stubbs, *The Constitutional History of England* (3d ed.), ii, p. 430.

Beside the general company of the staple to which we have referred, separate companies were incorporated in Ireland during the fifteenth and sixteenth centuries, the members of which were permitted to elect a mayor and two constables, to make by-laws, to have charge of official weighings and to take recognizances.¹

The privileges thus granted to the staplers were largely the result of merchandising privileges previously granted to foreign merchants of the Hanse towns. These were ever a fruitful cause of complaint among the English merchants,² and the early beginning of the staple may be ascribed to their desire for protection. One group of English merchants seem to have united under the name of "Fraternity of St. Thomas à Becket" and to have fixed their staple for woolen cloth at Bruges, where they received privileges from the court of Flanders and a charter from Henry IV (1406).³ During the fourteenth and fifteenth centuries, the fraternity levied tolls and exactions on English export to the Continent, to the great detriment of private traders. Their activities were no longer restricted to staple wares, but gradually extended to commodities in general. Notwithstanding complaints, a fresh grant of privileges was extended to them under the proud title of "the Merchant Adventurers of England." Under this charter, they were authorized to hold courts and marts at Calais, but were required to permit freedom of trade, subject to certain fixed exactions.⁴

¹ Gross, *op. cit.*, p. 146.

² Keutgen, *Die Beziehungen der Hanse zu England* (1890), pp. 32-34.

³ Cawston and Keane, *The Early Chartered Companies* (1896), p. 21.

⁴ *Ibid.*, pp. 26-27. The Adventurers themselves laid emphatic claim to their origin in the earlier fraternity. This has indeed been controverted by recent authority, though without definite proof, and the provisions of certain charters seem rather confirmatory than otherwise.

From this time forth, the company had a prosperous career. The business with the Lowlands was practically in their hands until the Spanish invasion. When their charter of privileges was extended (1586) to Germany, they established a distributing center for the greater part of Europe at Hamburg, where the society continued until the beginning of the nineteenth century.¹

The success of the Merchant Adventurers in stimulating English trade in European ports induced other merchants to seek similar charters for enterprises in other parts of the world. The era of discovery had set in. For the purpose of trade with southern and central Russia, Queen Mary granted a charter, in 1554, to the "Merchant Adventurers for the Discovery of Lands, Countries, Isles, *etc.*," not before known or frequented by any English," which cumbersome title afterwards gave way to the "Russia Company." In quick succession, charters with similar privileges were granted, in 1579, to the Eastland Company, to trade in the Baltic, and to the Turkey Company, "to trade to Turkey."²

The transition from these types of "regulated" companies to that of the joint-stock company resulted not through any progress of juristic conception, but because of the nature of the commerce which the earlier type had gradually developed. "The forces by which they were brought into being were not dissipated, but only diverted into fresh channels."³ The regulated companies represented groups of free merchants trading subject only to

See Lingelbach, *The Merchant Adventurers of England, their Laws and Ordinances, with other Documents* (1902), pp. xxiii, 199.

¹ Lingelbach, *op. cit.*, p. 39.

² Cawston and Keane, *op. cit.*, pp. 34, 61, 69.

³ *Ibid.*, p. 11.

the "regulations" of the society. They were indeed but a modification of the craft guilds, adapted to foreign instead of domestic commerce. Membership was by no means purchasable by mere contributions of capital, but was the result of a long apprenticeship and of other necessary personal qualifications.¹ Membership was not transferable nor could a member withdraw his share of the funds without due notice; furthermore, each member was liable to the whole extent of his means for the debts contracted by the company.²

It was undoubtedly due to these restrictions and the necessity for a more liberal employment of capital that the regulated system fell into abeyance. Well might the pleaders for the joint-stock principle, in 1681, say that "it cannot be denied by a reasonable man that a joint stock is capable of far greater extension as to the number of traders and largeness of stock than any regulated company can be. Because in a joint stock, noblemen, gentlemen, shopkeepers, widows, orphans, and all other subjects, may be traders and employ their stock therein; whereas in a regulated company, such as the Turkey Company is, none can be traders, but such as they call legitimate or bred merchants."³

The spirit of the times demanded a change in the form of commercial organizations. The Tudor period had developed internal concentration and a strong national consciousness. The regulated companies tended to become exclusive, a condition inconsistent with ambitious plans for

¹ Cawston and Keane, *op. cit.*, p. 10.

² *Ibid.*, p. 12. The joint-stock principle eliminated the necessity for apprenticeship by reason of the unrestricted assignability of the shares.

³ *Ibid.*, p. 13. "The equipment for the India trade required a capital so large as a joint stock alone could afford." James Mill, *History of British India*, i, p. 50.

a commercial and political expansion national in scope. The discovery of America and the multiplication of voyages to the East Indies gave opportunity for enterprises of unprecedented magnitude. It was in response to the demand for a wider participation in the fruits of national expansion that the joint-stock principle gradually gained acceptance.

The East India Company, or "Governor and Company of Merchants of London, trading into the East Indies," as the charter of Elizabeth (December 31, 1600) described it,¹ appears to have been closely connected with the Levant, or Turkey Company, at the time of its formation; they seemed to have used a common minute book.² The first charter gave no indication of any unusual change in the method of organization. About 215 merchants were constituted "one body corporate and politic," with power to have corporate succession, to admit and expel members and the usual incidents. The company was granted a monopoly of trade in the East Indies and could give licenses to non-members.

From the first voyage (1601) to the eighth (1613) groups of members contributed varying amounts of capital for the particular enterprise, thus forming a "joint stock," in the profits of which the particular members shared *pro rata*. From 1612 onward, the contributions from members desiring to participate were placed in the hands of the governor and committees (directors), to be ventured in a series of voyages. Thus the "Company's First Joint Stock" was devoted to four separate voyages from 1613 to 1616; successively other joint stocks were formed with

¹ Cawston and Keane, *op. cit.*, p. 87.

² Davis, *op. cit.*, ii, p. 114 note, citing Hewins, *English Trade and Finance*, p. 37.

different subscribers and upon somewhat varying conditions. This resulted in confusion, as the voyages of the preceding joint stock had not been completed before new joint stocks were created, while each joint stock had its own proprietors and board of directors.¹

The charter of Elizabeth does not of itself give evidence of the transition from the regulated type, with its element of separate undertakings and lack of unity, to that of a joint stock with all the adventures embraced in a single "voyage," enuring to the common good of all the subscribers. No mention is made of a fixed capital, nor even of shares. The enlarged powers given to the directorate may, indeed, be taken as indicative of a tendency toward greater unity. All ventures in the nature of contracts, operations of factories, acquisition and exploitation of lands, were to be undertaken in the name of the company. The principle of participation by stock, however, was a result of *internal* development, not of legislative (executive) intent. Bruce lays the adoption of the joint-stock plan to "the evil consequences of internal opposition."² It is not at all improbable, however, that the example of the Dutch East India Company had been observed and its advantages in practice already demonstrated. The charter of the Dutch Company proclaimed the joint-stock principle in the method by which it provided for accounting to its subscribers. Its organization under the

¹"Afterwards the directors had in their hands, at one and the same time, the funds of several bodies of subscribers, which they were bound to employ separately, for the separate benefit of each; . . . they, as well as their agents abroad, experienced great inconvenience in preserving the accounts and concerns separate and distinct . . ." Bruce, *Annals of the East India Company*, cited in Davis, *op. cit.*, p. 110. See also Mill, *op. cit.*, p. 44.

² *Op. cit.*, i, p. 162.

chamber system was, as we have seen, more decentralized than that of the English Company. But while the operation of the various ventures were conducted separately by the Dutch Company, each chamber was responsible for its profits and losses to the central board.

The short period of the English voyages, however, and the succession of joint stocks, taken together with a looseness of accounting caused a conflict of interests as between the various joint stocks of the English Company. The confusion of the several joint stocks related not only to the keeping of accounts and the distribution of the profits, but even to the right to exercise jurisdiction over territories occupied by the company as a result of the voyages; also to the right to share in acquests not strictly associated with mercantile ventures.¹

This condition threw serious doubt upon the wisdom of the joint-stock plan. Furthermore, merchants interested in some of the various joint stocks obtained from James I, in 1604, and from Charles I, in 1635, licenses to trade in parts of the Indies in which the old company had not settled any factories. One of these bodies, known as the Assada Merchants, united their interests for a time with the old company, in subscribing to a "united" joint stock. It is not known whether the directors were thereafter chosen by the contributors to all the separate stocks, or whether the contributors to each fund met separately.² We do know, however, that certain groups of contributors were dissatisfied with the exclusively corporate nature of the joint-stock principle and petitioned for a return to the plan of the regulated companies and freedom of trade among the members. This demand was refused by Crom-

¹ James Mill, *History of British India* (1817), vol. i, p. 52.

² *Ibid.*, i, p. 48.

well, but it had its effect in a plan for "a prodigious improvement on the preceding confusion and embarrassment, when several stocks were managed and as many contending interests pursued at once."¹ The holders of the old joint stocks were bought out by the company, and such as would not sell had their accounts carried forward to the credit of the united issue, after a specified term; on what basis, however, does not clearly appear.

Upon the accession of Charles II, a new charter was granted (1661) confirming the exclusive privileges, but further democratizing the joint-stock plan. Though the capital still remained variable and not divided into equal units, the shares were made transferable "even to such as were not free of the Company, upon paying £5 for admission."² Later (1693), a further modification was made in placing a definite limit of twenty-one years upon the duration of the joint stock, during the last year of which period books for the continuance of the joint stock were to be kept open.³

It is unnecessary to pursue the history of the company further, except to point out that henceforth Parliament began to claim the right of controlling the exclusive privileges granted by the Crown and to grant charters of a similar nature to rival companies.

A charter was granted (1698) to a rival group of financiers who had subscribed a government loan of two millions sterling. The constitution and powers of the new company, which bore the title of "General Society of Traders to the East Indies," were almost identical with the old. In fact, the two companies soon merged under the title "United Company of Merchants in England trading to the East

¹ James Mill, *op. cit.*, ii, p. 55.

² *Ibid.*, ii, p. 57.

³ Davis, *op. cit.*, p. 129, citing *Letters Patent Granted to the East India Company*, pp. 141-151.

Indies," and the older company surrendered its charter to the Crown.¹

The history of the East India Company may be taken as typical of other companies formed upon the joint-stock plan. Charters were granted by James I upon a joint stock to an African Company, in 1618, and successively, three more charters were granted to companies for similar purposes by James I and Charles I. These companies, with the Hudson Bay Company, chartered in 1670, also grew out of association types of regulated companies. Their main purpose was territorial or colonial development, rather than direct commercial profit, and by degrees their functions, operating under corporate form, became more and more governmental.

Joint-stock companies were created for the purpose also of carrying on *domestic* enterprises such as mining and manufacturing, as early as the sixteenth century. Originally, mining was conducted by organizations similar to the Continental *Gewerkschaften*. "The Society of Mines," authorized in 1651, was formed with the object of more effectually carrying out an industrial community of interest among its members. The capital consisted of twenty-four "parts," each selling at a different price.² Later, the type of mining association became quite similar to that of the colonial joint-stock company. In 1691, a charter was granted to the "Governor and Company of Copper Miners in England." An annual meeting was provided for, at which the shareholders were permitted to elect a governor, deputy governor and ten or more "assistants." The shares were issued in aliquot parts. Votes were required to be in

¹ Cawston and Keane, *op. cit.*, pp. 116-119.

² Scott, *The Constitution and Finance of English, Scottish and Irish Joint Stock Companies, 1720* (1910), ii, p. 383.

writing and any member whose calls were in arrear was subject to disenfranchisement.¹

A noteworthy step in the development of the English corporation type is represented in the charter and practice of the Bank of England. The early chartered companies were expected to prove advantageous to the government by providing money in large amounts at short notice. Thus, both the colonial and the domestic companies, besides being trading organizations, were also much against their will compelled to act as financial agents and provide the government with short-term loans. It was the need for government funds, taken together with the weakness of private banking institutions and the consequent failure of merchants to obtain grants of credit at reasonable rates, which led to the organization of the Bank of England.²

Differing from the East India and other early charter companies, the Bank of England was incorporated by Act of Parliament (1694). The total amount of capitalization was £1,200,000, consisting of one hundred pound shares, it being provided that no person could subscribe for more than £10,000, or hold more than £20,000. The bank was precluded from owing more than the amount of its capital, on pain of rendering the individual stockholders liable for thrice the amount so borrowed. It was not to trade in merchandise, but might lend on the security of merchants.

While prior to this time the members of the managing board were more frequently referred to as "assistants" or members of "the Committee," the official term of "director" now made its appearance, the qualification being the holding of stock of at least £2,000. Only one vote was permitted to any stockholder, irrespective of the amount

¹ Scott, *op. cit.*, p. 430.

² *Ibid.*, iii, p. 199.

of stock held by him, but a minimum holding of £500 was required in order to entitle the shareholder to vote. Not more than two-thirds of the directors retiring in any year might be re-elected in the following year. The charter was granted in 1694, and was to terminate in nine years.¹

The corporation type of the Bank of England set the standard for English companies by reason of the success which the venture attained almost from the start. The beginning of the eighteenth century saw a period of great activity in corporate enterprise and was accompanied by tremendous speculation in shares. This was fostered by the fact that from the reign of William and Mary it was customary for individuals to carry on business with capital stock and under corporate forms without obtaining a charter from the Crown. Under the common law, all such organizations were probably regarded as mere partnerships without the privilege of limited liability, although Maitland says that "very little is known as to how their affairs were regarded by lawyers and courts of law."² Numerous companies were formed in this manner between 1692 and 1695, and their existence was tolerated for the time being.

The active speculation going on at this period in the shares of these non-incorporated companies awakened the jealousy of the directors of the South Sea Company. This was the first great private company for foreign trade that had not had previous development as a regulated company.³ Though ostensibly organized for foreign trade,

¹ Scott, *op. cit.*, p. 205.

² *Collected Papers*, 1911, iii, pp. 389, 390. Lindley states: "By the common law, every association of persons formed for the sake of sharing the profits is either a partnership or a corporation—a company which is neither a partnership or a corporation is a thing unknown to the common law of England." *On Companies* (6th ed.), p. 2.

³ Davis, *op. cit.*, ii, p. 155.

its activities became financial rather than industrial. In 1720, its directors, in aid of the speculation in which they themselves were engaging, sued out writs of *scire facias* against a number of unincorporated companies with the view of discouraging speculation in their shares and in the hope that attention would thus be centered on those of the South Sea Company. Greatly to the chagrin of the South Sea Company's directors, however, this unexpectedly forced marginal holders of the unincorporated companies' stock to part with their securities in the South Sea Company. Thus the "South Sea Bubble" finally burst and a disastrous panic ensued.

In the same year, Parliament passed the "Bubble" Act, prohibiting the operation of unchartered joint-stock associations with transferable shares.¹ From this time forward, Parliament grew more and more jealous of the unrestricted functioning of the corporate type and gradually assumed to control it by general Acts. This legislation is described in a subsequent chapter.²

¹ The Bubble Act was extended over the American Colonies in 1741. Some of the Colonies owed their existence to charters granted by the Crown to trading companies. During the colonial period only six business corporations were organized of a strictly American origin or character, all of them following the plan of the early English chartered type. Baldwin, "American Business Corporations before 1789," in *Annual Report of American Historical Association*, 1902, vol. i, pp. 255 *et seq.*

² Chap. v.

CHAPTER IV

PROTECTION OF CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE—ORGANIZATION

I. FRANCE

Legislative Development.—The Napoleonic *Code de commerce* of 1807 was the first general statute to regulate corporations as independent legal entities. Its provisions were, however, of the most fragmentary nature. The arrangement of the articles as well as the terminology employed indicate that the legislator considered the corporation (*société anonyme*) merely as a species of limited partnership (*société en commandite*), wherein *all* participants were protected by limited liability. The articles of the Code applicable to the former are intermingled with those of the latter as well as with simple partnership (*société en nom collectif*) under the general heading "*Des sociétés*."¹

The French Code was probably the first general statute to provide expressly that "the members are liable only for the loss of the amount of their interest in the company."² The capital of the corporation was divided into shares of equal value, registered or payable to bearer.³ Differing from companies of the Dutch type, no preference was given to the large shareholders as such in respect of the right to become directors. The mandate of the directors was revocable.⁴ Nothing was provided as to the meetings of

¹ See *Code de comm.*, arts. 19, 29-38, 40, 45.

² *Ibid.*, art. 33.

³ *Ibid.*, arts. 34, 36.

⁴ *Ibid.*, art. 31.

stockholders nor as to their rights in general. The concessionary principle still prevailed and, accordingly, the administrative authorities exercised a certain control, especially over the articles of association.¹

Whenever this administrative control was relaxed, we find that both creditors and shareholders suffered severely. Thus at the beginning many speculative ventures, instead of being incorporated, were floated in the form of limited partnerships (*sociétés en commandite par actions*) for which no governmental authorization was necessary. The only partner whose liability was unlimited was usually a dummy.² The evils resulting from the use of this form finally led to the enactment, in 1856, of a special law.³ Shortly afterwards, in 1863,⁴ greater encouragement was given to the organization of strictly corporate types by dispensing with governmental authorization for limited companies (*sociétés à responsabilité limitée*) after the pattern of the English Companies Act of 1862.

The evils of overspeculation soon called for more drastic provisions. The Law of 1863 gave way to the more detailed Law of July 24th, 1867, which finally adopted the normative or non-concessionary system. This law, with certain modifications introduced by the Laws of August 1st, 1893, November 16th, 1903, and January 30th, 1907, still regulates corporations in France.

Existing Law.—The Law of 1867, dispensing with governmental authorization, prescribes certain formalities compliance with which *co ipso* constitutes the entity in law.⁵ These requirements may be briefly stated as follows:

¹ Lyon-Caen and Renault, *Traité de droit commercial*, ii, no. 669.

² Lehmann, *op. cit.*, i, p. 71.

³ L. of July 17, 1856.

⁴ L. of May 23, 1863.

⁵ Art. 21.

1. No company may be organized with less than seven members.¹

2. The shares must be in denominations of at least 25 francs, if the entire capital does not exceed 200,000 francs and of at least 100 francs, if the entire capital exceeds this amount.²

3. The entire share capital must be subscribed,²

4. Shares of a denomination of 25 francs must be entirely paid up and those of a higher denomination must be paid up to the extent of at least one-quarter.²

5. The subscription and payments must be verified by the organizers and to this verification must be annexed the agreement of organization.²

6. Although bearer shares as well as registered or nominative shares are permissible,³ the shares must remain nominative until fully paid up.⁴ Vendors' (*apporteurs*) shares must be fully paid up before the corporation is completely organized. They must remain in the treasury, and are not negotiable until two years after the complete organization of the corporation.⁴ The Law of August 1st, 1893, compels directors, during this interval, to see that the partly paid and vendors' shares are stamped so as to indicate their character as such and the date of organization. The holders, the intermediate transferees and the original subscribers are all made jointly and severally liable for the balance unpaid upon the shares. But subscribers or stockholders who have transferred their shares cease to be liable for calls made more than two years after such transfer.⁵

¹ Art. 23.

² Arts. 1, 24.

³ *Code de comm.*, arts. 35, 36.

⁴ L. 1867, arts. 3, 24, as amended by L. 1893, art. 2.

⁵ *Ibid.*

These provisions are protective of the stockholder who has fully paid his subscription and inure to the benefit of creditors also, as they are thus enabled to trace transfers of the stock and identify the new holders for at least a period of two years from the time of organization. The vendors remain liable during this period, so that the fact of full payment may be questioned without having to proceed against the new transferees, who may prove to be irresponsible.

These provisions have an intimate connection with the rules governing *apports*, or contributions in property, which we discuss *infra*. It is remarkable, however, that, having gone so far, the legislator failed to designate any period within which calls to the full extent of the capital must be made.

7. The *apports*, or transfers of property by the vendor-organizers in payment of subscriptions, also all other agreements for the special advantage of organizers (such as percentages on profits, salary agreements, *etc.*), must be approved by the first meeting of stockholders. Thereafter, a second meeting must be held, at least five days before which a printed report relating to the *apports* or other particular advantages shall have been placed at the disposal of the stockholders. The resolution of approval must be passed by a majority of stockholders present, representing at least one-half of the capital stock. The organizers interested in the resolution are disqualified from voting. In default of such approval, the organization is void in respect of all parties. But the confirmatory resolution, if passed, does not prevent an action on the ground of fraud.¹

The object of these provisions is to prevent promoters from selling at inflated values, and from burdening the

¹ L. 1867, arts. 4, 24, 30.

corporation with unfair contracts for salaries and the like, omitted in the prospectus. We shall see how the same evils are dealt with in the most recent legislation of England by provisions relating to the prospectus itself.¹

8. Within one month from the date of organizing the corporation, a duplicate, or (if verified by notarial act) a copy, of the articles of association must be filed in the office of the justice of the peace or tribunal of commerce of the district in which the corporation is established. To this must be annexed (a) a copy of the subscription and proof of payment of at least one-fourth; (b) a certified copy of the resolutions passed at the general meeting (required in the case of *apports* of property); (c) a certified list of the name, address and occupation of each subscriber and the number of shares subscribed for.²

9. Within one month, an extract of the articles of association must be published in the official journal, the advertisement to contain the title and duration of the corporation, its principal office, the name and address of the persons entrusted with its management and the power of signature, the amount of money or property to be contributed, the date of beginning business, and the date when the documents were officially filed.³

Comment.—The Continental systems, differing from those of England and the American states, lay stress upon the importance of obtaining subscriptions to the entire amount of the authorized share capital before the corporation is authorized to do business. This may be accomplished by simultaneous act or by a series of successive acts. French law, differing from that of Germany, does not especially provide for a simultaneous and complete subscrip-

¹ *Infra*, chap. v, tit. "Over-capitalization."

² L. 1867, art. 55.

³ Arts. 56, 57.

tion (*souscription intégrale*), although the method is sometimes followed in practice. The method contemplated by statute is by open offer to the public continuing until the capital is completely underwritten. Meanwhile, the corporation is denied the right to do business. If a rigorous enforcement of this prohibition were made and adequate sanction provided for the protection of money stockholders against the possibility of fictitious subscriptions, the system would be admirable in assuring economic strength to the corporation before commencing to operate. We shall see that these sanctions are more adequately provided under the German system than under the French.

A specific provision, no matter how clear or categorical, is ineffective unless accompanied by a device for its enforcement. This is evident especially in respect of the French provisions designed to prevent the overvaluation of property transferred to the corporation in payment of subscriptions. The nullity of the corporation is stated to be the penalty of an original organization in which some of the subscriptions have been paid in property at a fictitious valuation. Nullity will be decreed, however, only in the event of fraudulent intent, and the difficulty of proving fraud to the satisfaction of a French tribunal is regarded by some as one of the chief dangers threatening confidence in corporate organizations in France.¹

The privilege extended to any of the organizers by the articles of association to pay for their subscriptions in property tends to destroy equality among the shareholders from the very beginning. The system introduced to prevent this by the Law of 1867 seems ingenious, and the cause of its failure is not at first apparent. The shareholders who pay for their subscriptions in money are made the arbiters of the value of property brought in

¹ Nouel, *Les Sociétés par actions; la Réforme* (1911), p. 128 and note.

(*apportée*) by other stockholders. The value of the property may be lawfully certified by resolution of these subscribers only after the report made thereon by experts designated by the money subscribers. The system is thus theoretically just and fair; yet recent writers do not approve of its practical results, for the reason that a critical appraisal is rarely made. The stockholders seldom reject a valuation suggested by the promoters. At most, the money stockholders delay their approval for a time, during which negotiations ensue between themselves and the *apporteurs*. This usually results in a compromise by which the money stockholders receive additional consideration in stock (*i. e.* a bonus) without strengthening the financial condition of the corporation.

Another cause for the failure to control the valuation of property transferred is due to the fact that the money stockholders are frequently interested in syndicates promoted in conjunction with the *apporteurs*, with the object of ultimately placing the stock with the public. Accordingly, the original shareholders have but little interest in proving the value of the property contributed. The appraisers often make their report solely upon information furnished by the organizers. Indeed, at the Corporations Congress of 1900, Rousseau stated that the report was frequently made *after* the articles are executed.¹

The chief restraint upon indiscriminate overvaluation of property transferred in payment of subscriptions lies in the provision of the Law of 1893 prohibiting the negotiation of shares paid for in property during a period of two years.² This has somewhat discouraged the flotation of *apporteurs'* shares. It fails, however, to cure the evils we have described, operating to the detriment of bona-fide

¹ *Congrès des sociétés de 1900*, p. 78, cited Nouel, *op. cit.*, p. 133.

² Law of August 1, 1893, art. 2, amending Law of 1867, art. 3.

money subscribers. It also fails to protect creditors who are induced to extend credit to the corporation in the belief that the capital has been fully paid in.

Furthermore, many provisions of the Law of 1867, as modified by that of 1893, though salutary in themselves, are not applied rigorously by the French courts. Notwithstanding the provisions of article 15, visiting the penalties of criminal deceit upon those who publish false statements for the purpose of obtaining subscriptions, the courts have not applied the article to exaggerations and misrepresentations contained in the prospectus. Thus in one case the court said that certain representations "regrettable indeed as they were, did not transgress the limit of those adventurous statements and even falsehoods which are frequently met with in commercial prospectuses;" "that mere false statements, however multiplied, do not of themselves constitute fraudulent practices in the sense of article 415 of the Penal Code."¹

Another defect admitted by modern French writers is that the Law of 1867 does not provide for immediate responsibility of the organizers or managers in the event of a violation of the provisions relating to corporate organization. Their responsibility results only indirectly from a judgment declaring the corporation a nullity. Furthermore, the adjudicated cases show that a judgment of nullity is rarely decreed until long after the time when the corporation begins to do business. During this period the money of the cash subscribers has been transformed into dead capital, such as machinery, merchandise, *etc.* Debts have been incurred in the purchase of property, or in defraying the running expenses of the business.

As against creditors, neither the corporation nor the

¹ Trib. of Commerce, Paris, Mar. 23, 1887, Dalloz, 1887, part ii, p. 251.

stockholders can set up the defense of nullity.¹ Accordingly, creditors have the option of treating the corporation as null, or as validly constituted. If they choose the latter, the evil day is postponed; if the former, the court is compelled to deal with a corporation in fact, if not in law, and must proceed to liquidate by selling the assets and distributing the proceeds. If action has not been too long delayed, the creditor may suffer little, if any, loss. The money stockholder, however, is met with the principle of French jurisprudence that the court has no power to distribute the assets otherwise than as agreed upon by the parties themselves, notwithstanding the nullity of the corporation. For example, where the court has annulled a corporation for violation of article 1 by reason of the share capital not being fully subscribed, or by reason of the subscriptions not being paid in to the extent of one-quarter, the shareholders who have contributed property cannot be compelled to take back their *apports*, but may participate in the proceeds of all the assets to the same extent as the other subscribers.² Accordingly, the creditors and money stockholders, who are entitled to the greatest amount of protection, have the least incentive to avail themselves of the sanctions provided for by the law and intended for their benefit.³

The action of nullity is employed only as a condition precedent to holding the organizers or managers responsible for a violation of either formal or substantial provisions. It is a proceeding relied upon as a formality, very much as judgments are obtained against corporations under English and American law and prosecuted to execution where

¹ Art. 7, L. 1867.

Nouel, *op. cit.*, pp. 119-122.

³ Marinesco, *Des Conditions exigées pour la constitution des sociétés anonymes* (1889), p. 220. This author is of the opinion that the Law of 1867 has failed in the protection of creditors and later shareholders.

there is no dispute and no possibility of realizing, but where all legal remedies must be exhausted as a technicality demanded by equity courts prior to proceedings against directors for malversation of corporate funds.

Thaller has said that the action of nullity is frequently used as a sword by unscrupulous persons to compel recognition of doubtful claims.¹ It is true that under the Law of 1893, this evil has been mitigated by introducing a short statute of limitations. The law also permits the cure of defects prior to action brought. But close observers still regard the law as unnecessarily severe against the organizers. On this account, experienced and financially responsible persons often refrain from undertaking the organization of corporations. This works injuriously and not beneficially in the interests of creditors and stockholders. The action of nullity might well be replaced by measures more effective though less severe. Responsibility for compliance with the law should be made independent of the action of nullity, and original money subscribers should be protected against inflated contributions of property.

2. GERMANY

Legislative Development.—The Napoleonic codes were extended, in 1807, to Baden, the Rhenish Palatinate, Rhenish Hesse and the Prussian provinces of Posen, Rhenish Prussia and Westphalia. Despite the fall of the French Empire, they continued in force until replaced by German legislation. Accordingly, the corporation type of the *Code de commerce* exerted important influence upon all subsequent legislation in Germany. Prussia was the first state of Germany to provide separate legislation for general corporate regulation, at first in respect of railroad corporations² and afterwards for all corporations.³ Austria,

¹ *Journal des sociétés*, 1884, p. 764.

² L. of November 3, 1838.

³ L. of November 8, 1843.

Hamburg, Saxony and Bremen still continued to pass laws relating only to certain specific questions of corporation law. Saxony had in preparation a draft of a general law during 1836 and 1837, but it was not adopted.¹

After 1838, the commercial requirements of the German states led to the preparation of a number of drafts for a commercial code. The Wurtemberg draft of 1839, the Prussian draft of 1857, the Austrian draft of 1858 and the so-called Frankfort draft of 1859 all contained provisions relating to corporations and followed the type established by the *Code de commerce*, with the distinguishing characteristic of limited liability.

The basis of the modern German law of corporations is to be found in what is now known as the Old Commercial Code, adopted in 1861 in most of the German states—separately, but in an uniform text. It was the result of a conference for uniform commercial legislation called by Bavaria in 1856, held at Nuremberg. The draft prepared by the conference was adopted as a federal statute of the North German Confederation² and, two years later, as a federal statute of the German Empire.³ In the meantime, a special statute had been passed, amending the code in respect of corporations,⁴ the principal characteristic of which was the definite adhesion to the free or non-concessionary principle. Theretofore, corporate entity had proceeded from a public act of the state (*constitutio personalis*); thereafter, it resulted from the observance of normative regulations laid down by general statute.

The abuse of corporate forms as instrumentalities of business and the panic of 1873 which resulted partly there-

¹ Lehmann, *op. cit.*, i, pp. 77-78.

² L. of June 5, 1869.

³ L. of April 16, 1871; for Bavaria, April 22, 1871.

⁴ L. of June 11, 1870.

from, led to the demand for a stricter regulation of corporate organization.

The ministry of justice prepared a draft statute which was presented to the federal council on September 7th, 1883.¹ The draft was finally adopted by the Law of July 18th, 1884.

A final revision of the Commercial Code was made as part of the series of federal laws passed just prior to the opening of the present century, designed to unify and modernize the entire private law of Germany. The provisions of the Commercial Code had to be brought into harmony with those of the new Civil Code, and, accordingly, a draft was presented in July, 1896, when the Civil Code was adopted by the Reichstag. A second draft, in line with suggestions made in the Reichstag, was presented at the next session and became a law on May 10th, 1897.²

In the Commercial Code thus revised in 1897, the provisions relating to corporations³ grew much more detailed. The principal additions are those which provide for a more thorough *administrative* control over organization, increase and decrease of capital stock, transfer in bulk of the entire property of a corporation and proceedings for dissolution.

Corporations under German law are distinguished from associations with limited liability (*Gesellschaften mit beschränkter Haftung*), provided for by the law of April 20th, 1892. These organizations, which play an important part in the commerce of Germany at the present day, may

¹ The draft was thoroughly digested and criticized by Goldschmidt in *Zeitschrift für Handelsrecht*, vol. xxx; by Bähr in *Ihering's Jahrbücher*, vol. xxi; and by Wiener, *Der Aktiengesetz-Entwurf von 1883*.

² Staub, *Kommentar zum Handelsgesetzbuch*, i, pp. 1-2.

³ Secs. 178-319.

be compared to limited partnerships in which *all* of the parties are limited partners. The company represents a separate juristic entity,¹ but the share capital is not divided into shares of stock and no part is transferable without the consent of the company.² Accordingly, this type will not be treated of in the succeeding pages.³

Existing Law.—The German Commercial Code (*Handelsgesetzbuch*) does not provide a definition of corporations. It simply outlines the prerequisites for the existence of a corporation and defines the legal relations of parties interested as organizers, stockholders, or creditors.

The provisions of the Code are contained in a separate division entitled "*Aktiengesellschaften*."⁴ In order to form a corporation under German law, at least five persons must verify articles of association in the presence of a court, or notary, subscribing for a certain number of shares. The articles must contain:

1. The name and the *situs* of the corporation.
2. The purposes for which it is organized.
3. The amount of capital stock and the par value of the shares.
4. The officers to be elected and the manner of their election.
5. The manner in which the general meeting of stockholders is to be called.
6. The manner in which official notice by the corporation is to be given.⁵

As in the French Code, a general provision declares

¹ L. of April 20th, 1892.

² *Ibid.*, sec. 17.

³ See generally upon these organizations, Staub, *Kommentar zum Gesetz betreffend die Gesellschaften mit beschränkter Haftung* (1909).

⁴ German Comm. C., secs. 178-319.

⁵ *Ibid.*, sec. 182.

that all stockholders are limited in their liability to the amount of their shares.¹

Differing from the practice in England and the United States, bearer shares are customary; accordingly they are expressly recognized by statute.² Fractional shares are not permitted. As bearer shares can be freely negotiated without transfer on the books of the corporation, the holders of such shares are not known to the corporation until the coupons attached have been presented for the payment of dividends declared. Accordingly, the legislature, in order to insure full liability of the shareholder up to the amount of the price agreed to be paid for his shares, has prohibited the issuance of bearer shares of which the subscription price has not been completely paid in. This is required even in cases where the amount agreed to be paid for the shares is greater than par. Registered shares on which only part payment has been made, must contain a statement on the face of the certificates, of the amount paid.³

A notable provision of the law requires all shares to be of a par value of at least one thousand marks, except in certain special cases not necessary to mention, in which the shares must be of the par value of at least two hundred marks.⁴ This provision is intended to discourage speculation by persons of limited means; accordingly, there is now but little speculation by the working classes in shares of small denominations, so frequently encountered in mining and other companies in England and America.⁵

¹ German Comm. C., sec. 178.

² *Ibid.*, sec. 179.

³ *Ibid.*, sec. 179.

⁴ *Ibid.*, sec. 180.

⁵ Modern German writers point to the fact that the very class least able to bear the burdens of loss through reckless or fraudulent issues of securities is often the first to become interested in them. Böhm, *Ueber Aktionärschutz nach deutschem, englischem und französischem Recht* (1910), pp. 44-45.

The articles of association serve both as a subscription agreement and as a constitution or organic law of the corporation. The Code mentions only the *minimal* requisites of the articles of association. It is customary to include in the articles a detailed regulation of the internal organization of the corporation under the heading of "*Statuten*." Such statutes or regulations establish the powers and compensation of the supervising council (*Aufsichtsrath*) and directorate (*Vorstand*), the object and duration of the corporation, the powers of the stockholders in general assembly; the nature and value of the business or property to be turned over to the corporation in payment, in part or in whole, of subscriptions not payable in cash; and many other provisions which are found both in the certificate of incorporation and by-laws of corporations organized under English or American practice.¹

If the articles do not state the character of the shares, they are deemed to be nominative. The articles, however, may provide that, upon the demand of a stockholder, shares which are nominative may be made bearer shares and those which are bearer shares may be registered in the name of the owner.²

The articles may also provide for the classification of the stock, preferred and common. The Code does not state all of the varying rights which may be provided for by the articles. It recognizes varying rights in the division of profits and capital;³ it also recognizes that the articles may provide a maximum of shares upon which any one stockholder may vote; that certain classes of stockholders, as for instance, holders of preferred stock,

¹ See, for example, Senftner, *Wie gründet man eine Aktiengesellschaft?* p. 17, where a form of articles is given.

² Comm. C., sec. 183.

³ *Ibid.*, sec. 185.

may have greater voting capacity than those of a different class.¹ Accordingly, German law gives a free hand in all matters of varying agreement by which minority shareholders may be protected and by which preferential and proportional voting may be effected.

German law differs from the French in its method of dealing with purchases of property. Where contributions in kind are permitted by the articles, it is customary to speak of a "qualified" organization (*qualifizierte Gründung*).² The Code requires the articles of association to state the particular advantage which any individual stockholder (mentioning his name) is to receive. Payments made by stockholders upon the capital stock otherwise than in money, with the name of such stockholders, the basis of payment and the number of shares thus issued must be stated in the articles.³ All agreements of this character not specifically set forth are invalid as against the corporation.

German law is peculiar in providing a definition of persons to be regarded as organizers (*Gründer*). The Code provides that stockholders who adopt the articles of association, and those who pay for their subscription otherwise than in money, shall be regarded as (*gelten als*) the organizers of the corporation.⁴ The purpose of this definition is to identify the persons upon whom the legislature elsewhere places the burden of responsibility under penalties both of a civil and of a criminal character.⁵

The execution of the articles of association does not in

¹ Comm. C., sec. 252; see Staub, *Kommentar zum Handelsgesetzbuch* (1900), i, pp. 760-1.

² Gierke in *Holtzendorff's Encyklopädie der Rechtswissenschaft* (1904), i, p. 948.

³ Comm. C., sec. 186.

⁴ *Ibid.*, sec. 187.

⁵ Staub, *op. cit.*, i, p. 578.

itself constitute the corporation a legal entity. All of the authorized capital stock must be subscribed for before the corporation is authorized to do business. Two methods of accomplishing the subscription in full are provided for. The first is that by which the organizers subscribe for the entire capital stock in the articles.¹ This is by far the most usual proceeding and is known as "simultaneous" organization (*Simultangründung*).

The second method is complicated and is seldom employed in practice.² It is known as successive organization (*Successivgründung*) and consists in obtaining subscriptions during a period of time after the signing of the articles, until the capital stock is completely subscribed for. The document of subscription (*Zeichnungsschein*) consists of a written declaration containing reference to the date of the articles of association, the name, occupation and residence of each organizer, the subscription price of the shares and payments to be made thereon, and the date at which the subscription shall become invalid if the entire amount has not been underwritten.³

If the organization is simultaneous, the organizers designate the first supervising council in the articles, or by separate document verified in the presence of a court or notary.⁴ If the organization is successive, the supervising council must be elected at a general meeting of the stockholders after the capital stock has been completely subscribed.⁵

Beside the supervising council, German law provides for a directorate (*Vorstand*) consisting of one or more persons to be appointed in the manner provided for in the articles. If the articles provide for the appointment of the

¹ Comm. C., sec. 188.

² Senftner, *op. cit.*, p. 11.

³ Comm. C., sec. 189.

⁴ *Ibid.*, sec. 190.

directorates through the general meeting of stockholders, the first board is appointed in the same manner as the supervising council.¹

As a further protection to the public against the flotation of watered securities, the new Commercial Code has introduced a somewhat novel guarantee of the good faith of the organizers. Whenever subscriptions are to be paid otherwise than in cash, the organizers must sign a declaration stating the essential circumstances which tend to show the reasonableness of the agreement so far as the same relates to the acceptance of property instead of cash. This declaration must set out the transactions by which the company came to acquire the property and the average cost price over a period of two years. If the company is to acquire the business of a going concern, the declaration must state the results of operating the same during the previous two years.²

After the election of the supervising council and the directorate, it is their first duty to examine and certify as to the legal organization of the company. If, however, any of the directorate or supervising council are likewise organizers, or recipients of any particular advantages or compensation by reason of the organization, or have transferred property other than money in payment of shares, the certification of the proper organization of the corporation must also be made by auditors (*Revisoren*) appointed by the official board of trade of the district, or in the absence of any such, by the court.³

The examination must relate particularly to the correctness and completeness of the declaration made by the organizers with reference to the subscriptions to and pay-

¹ Comm. C., sec. 190.

² *Ibid.*, sec. 191.

³ *Ibid.*, sec. 192.

ment of the capital stock. It must also relate to the facts constituting the basis for the declaration of the organizers with regard to the reasonableness of agreements to transfer property in exchange for shares. A report embodying the results of the examination must be made by the supervising council and directorate jointly, and, in the event that auditors have been appointed, they must also execute the report, a copy of which must be delivered to the board of trade which appointed them. The report is accessible to the public.¹

If differences arise between the auditors and the organizers as to the scope of the examination, the board of trade or court which appointed the auditors must determine whether the demand for further information is justified.²

All the foregoing provisions are reinforced by the requirements of publication demanded by the Code. The corporation must be registered as such in the commercial registry of the court of the district in which it has its *situs*, pursuant to an application signed by all of the organizers, members of the supervising council and directorate. The application for registration must include:³

1. The articles of association and subscriptions to the capital stock;
2. all contracts relating to special advantages and compensations of stockholders and organizers;
3. in the event that all shares are not subscribed for by the organizers, a duplicate of all subscriptions must be registered, together with a list of all subscribers and the amounts still owing on each share;
4. the documents relating to the election of directorate and supervising council.

¹ Comm. C., sec. 193.

² *Ibid.*, sec. 194.

³ *Ibid.*, sec. 195.

5. the report as to the legal organization of the corporation and the documents upon which it is based; if the report is made also by auditors, a certificate that a report of the auditors has been delivered to the board of trade;

6. whenever the particular nature of the undertaking requires governmental consent, a document showing such consent must also be filed.

The application for registration must also contain a declaration that every share has been paid for in money and that the directorate is in possession of the same, except such subscriptions as were agreed to be paid for in property. The price at which the shares were issued and the amount of money paid thereon must also be stated; this must be at least one-quarter of the par value and in the event of issuing shares at a price above par, at least one quarter of the actual price. The members of the directorate must send their signatures for filing with the courts; all documents presented with the application for registration must also be filed in court either in their original form, or by certified copies.¹

The registration of the corporation as provided for by law constitutes a condition precedent to the existence of the corporation as such.² Every person assuming to act in behalf of the association prior to its entry in the commercial register at the seat of the corporation will himself be personally liable, and no shares or interim certificates can be issued prior to that time, nor can any subscription right be transferred.

The organizers are responsible to the company as joint debtors for the correctness and completeness of the statements made in their reports relating to the subscriptions and

¹ Comm. C., sec. 195.

² *Ibid.*, sec. 200.

payments of the capital stock, and to the advantages which they or any stockholders are to receive, either directly, or through payment of subscriptions in kind. They are liable for all balances due on subscriptions and must take over any balance of stock remaining unsubscribed for. If the company has been injured by reason of their acceptance of property in payment of subscriptions, with fraudulent intent, all of the organizers are liable as joint debtors; provided, however, that if an individual organizer had no knowledge of the incorrectness or incompleteness of the statements made, or of an intentional injury to the corporation, or could not have known of it by exercising the ordinary care of a business man, he may be held free of liability.¹

Liability is incurred jointly with the organizers by any person who receives a benefit, as part of the cost of organization, not mentioned in the schedule of charges required to be published, provided he knew or must have known that such information was wilfully withheld; the same applies to all parties who knowingly withhold such information, or who knowingly aid in the wilful injury of the company by transfer of property in payment of subscriptions.²

The Code goes further than any prior legislation in protecting the public against fraud or negligence in the organization of corporations, by placing a liability even upon the bankers who offer the shares for sale. All persons who have made a public offering of the shares before the registration of the corporation or within two years thereafter shall be jointly liable with the organizers in case of the incorrectness or incompleteness of the report of the organizers relating to the subscription or payment of the capital stock, or to the advantages agreed to be given to

¹ Comm. C., sec. 202.

² *Ibid.*

certain of the shareholders or organizers, or in case of wilful injury to the corporation through payments in kind, provided such persons knew of the incorrectness or incompleteness of the statements, or of the wilful injury, or might have had such knowledge by the exercise of the ordinary care of a business man.¹

This practically makes the issuing banker a guarantor of the correctness of the statements made by the organizers in connection with their report for the registration, and requires him to make an independent investigation in order to be satisfied that all of the legal and economic requirements have been complied with. The provision is applicable also to all persons endeavoring to make sales by public offering of stock already issued and on the market, irrespective of the fact that they took no part in the original issue.² The statute is intended to prevent general distribution of shares regarding which the advertiser or banker may have little information. It is designed to prevent the irresponsible dissemination of worthless shares by puffing and extravagant promises.

In fact, the responsibility of the banker is in many respects placed on the same basis as that of the organizer. The Code makes both jointly liable to the company; indeed, redress must be sought against them before recourse is had against members of the supervising council or directorate, for any failure properly to verify compliance with the law. The latter become liable for their negligence only in the event that redress cannot be obtained from the organizers or the bankers.³

A cause of action against the organizers, issuing bank-

¹ Comm. C., sec. 203.

² Staub, *op. cit.*, i, p. 619.

³ Comm. C., sec. 204.

ers, members of the supervising council or directorate for failure to verify compliance with the law as already outlined, is prescribed after a period of five years from registration in the commercial registry.¹

Prior to the Law of 1884, it was not unusual for the organizers to enter into agreements disadvantageous to the company and, after the period of organization had been completed, effect a compromise of their liability. This was easily accomplished by reason of the fact that they were likely also to have a majority of the stock; thus, at the first general meeting of stockholders, they obtained the adoption of a resolution granting *décharge*.² It is now provided that no waiver or compromise of claims against any of the persons responsible for the proper organization of the company is permissible until after five years from the period of registration and then only by vote of a general meeting of stockholders; a minority of one-fifth of the capital stock may veto the resolution.³

A resolution of the general meeting of the stockholders is required for the acquisition within two years from the time of registration, of any equipment intended for permanent use in the business of the company, or of immovables exceeding in value one-tenth of the capital stock. Before the resolution is passed, the supervising council must examine and report in writing upon the proposed acquisition; and the resolution requires a majority of three-quarters of the capital stock represented at the meeting. If the contract is undertaken within one year from registration, the three-quarters majority must represent at least one-quarter of the entire capital stock. The resolution itself must in all cases be registered.⁴

¹ Comm. C., sec. 206.

² Staub, *op. cit.*, i, p. 624.

³ Comm. C., sec. 205.

⁴ *Ibid.*, sec. 207.

As a corollary to the obligation placed upon banks of issue, a further protection against reckless flotations of new and untried securities is found in the prohibition laid upon all stock exchanges from listing the shares of any corporation prior to one year from registration in the commercial registry and the publication of its first annual balance sheet and profit-and-loss account.¹

In addition to safeguards found in the method and procedure of organization, German law is characteristic in the precision with which it has provided for *criminal* penalties applicable to offenses committed by the organizers or others in connection with the organization of the company and the flotation of its securities.

The Commercial Code of 1870 added penal provisions in the division relating to corporations; it defined the offenses and punishments concretely instead of referring to the general provisions of the Criminal Code. These special provisions were amplified by the Law of 1884 and were incorporated, practically without change, in the new Commercial Code.²

Punishment by imprisonment and at the same time by fine not exceeding twenty thousand marks is imposed as a penalty upon:

1. organizers or members of the supervising council or directorate who, for the purpose of entering the corporation in the commercial registry, knowingly make false statements in respect of the subscription or payment of the capital stock, or of the price at which the shares are issued, or in respect of the payments of subscriptions otherwise than in money;

2. any persons who knowingly make false statements in respect of any of the foregoing matters in a prospectus publicly offering the shares of a corporation for sale;

¹ L. of June 22nd, 1896, relating to Stock Exchanges (*Börsengesetz*), sec. 39.

² Staub, *op. cit.*, i, p. 934.

3. members of the supervising council or directorate who, for the purpose of entering in the commercial registry an increase in the capital stock, knowingly make false statements in respect of the payment of the stock already issued, or of the subscription or payment of the increased stock, or in respect of the amount at which the shares are issued, or in respect of payments upon the increased stock made otherwise than in money.¹

In addition to the penalties already mentioned, managers and directors may incur the loss of civil rights. If, however, there be extenuating circumstances, sentence may be confined to the imposition of a fine.² Under the general provisions of the Criminal Code, the length of imprisonment may vary from one day to five years.³

Members of the directorate or supervising council are punishable with imprisonment not exceeding one year and also by fine not exceeding twenty thousand marks, if they have knowingly issued nominative shares, partly paid up, not mentioning the amount actually paid thereon; or issued shares or interim certificates before the company has been registered in the commercial registry; or issued shares or interim certificates of less than one thousand marks par value, as provided by law. These officers, and also liquidators, are subject to the same penalties if they have knowingly made false reports or statements as to the condition of the company's affairs. If there be extenuating circumstances, punishment may be restricted to the imposition of a fine.⁴

Comment.—The detailed and conservative nature of German legislation governing corporations may be ascribed to the severe experiences of the German people following the Franco-Prussian War. Their victory in that contest and in particular the large indemnity paid by France

¹ Comm. C., sec. 313.

² *Ibid.*

³ Secs. 16, 27.

⁴ *Ibid.*, sec. 314.

led to an enormous increase in commercial enterprise; it also gave opportunity, however, for dangerous speculation with which the existing laws of corporations were then ill-designed to cope. Ihering, writing in 1877, said:

The corporation in its present form is one of the most incomplete and dangerous devices of our entire jurisprudence. Most of the evil which has overtaken commercial relations during the past few years results either directly from this source, or is at least closely related to it. . . . The attacks which it has incited against private property have been more serious than if fire, drought, famine, earthquake, war and hostile occupation had all conspired to ruin the welfare of the nation.¹

When such was the warning of one of Germany's leading jurists, it is not surprising that every possible safeguard was thrown round the organization of corporations during succeeding revisions of the law.

The capstone of the structure provided by the new Commercial Code is publicity. Some authors, even in Germany, are of the opinion that the requirements of publicity have been somewhat overextended;² that the system has thus become ponderous and that those who would inform themselves of facts necessary for their protection are compelled to wade through a mass of material much of which could be dispensed with.

The express provisions of the Code are evidence of the fact that the legislature gave paramount consideration to the rights of the creditors and ordinary stockholders (as distinguished from the organizers). Thus it is provided that as soon as the organizers take over all of the shares, the company is organized (*errichtet*).³ And yet, before the

¹ Ihering, *Zweck im Recht*; translated from i, pp. 227-228.

² Rehm, "Die Uebertreibung des Offenheitsprinzips im Aktienrechte," *Deutsche Juristenzeitung*, 1904, pp. 34 et seq.

³ Comm. C., sec. 188.

organization of the company has been registered in the commercial registry at its *situs*, the corporation does not exist (*besteht nicht*) as such.¹ Just what is the legal nature of the organization in the meantime is not expressly stated in the Code. The best authorities are of the opinion that before registration, even though all other requisites have been complied with, it has no capacity to acquire rights or incur obligations, although as an association regulated by the Civil Code certain rights may accrue and certain obligations attach to its members as individuals, *i. e.* they may become joint creditors and joint debtors.² An act performed in the name of the association prior to its corporate existence is unqualifiedly stated to render the individual personally liable.³ What benefits, if any, may accrue to the organization during that period by reason of acts undertaken in its name are not made clear. It is manifestly intended to discourage all activity prior to full compliance. This is consistent with the system of issuing the stock which, as under the French code, must all be subscribed for before registration can be made. Thus economic strength is assured to its authorized capital; intending purchasers of stock and creditors know the amount which may be relied upon before the company is committed to liabilities and before any of the funds already contributed have been used as working capital.⁴

Gierke considers that the chief value of the scheme lies in the fact that an individual duty is laid upon all those charged with verifying compliance with the law, whether

¹ Comm. C., sec. 200.

² Staub, *op. cit.*, pp. 605-606.

³ Comm. C., sec. 200.

⁴ Cf. Gareis, *Das Deutsche Handelsrecht* (1909), p. 219; Böhm, *op. cit.*, p. 13.

as organizers or promoters, supervisors or auditors.¹ The distinction as regards rights and duties between subscribers who have undertaken to pay their subscriptions in kind and those who pay in money is taken over, with modifications, from the French Law of 1867; but the feature of verification by the supervisors of the corporation, if disinterested, or by auditors, if the supervisors are interested, is novel. Modern experience teaches that it is necessary to have some independent test in order to prove compliance both with formal requirements and with the demands of sound business finance. The organizers as well as the initial officers are frequently also the majority stockholders, or able to control a majority at the first meeting. Even if they do not, they usually have a sufficiently large interest in the taking over of property or entering into contracts to prevent an impartial judgment in these matters. It is important that the administrative device intended to remedy this should be free from great expense, complication or delay. We shall see that, in some countries, a judicial tribunal is clothed with the power to approve the various steps taken in organizing.² It is doubtful whether courts of law are so constituted as satisfactorily to perform duties of this nature, although some recent expressions of opinion tend in this direction.³ It is noticeable, indeed, that in the United States, especially within the past decade, questions of a business nature have been referred to or voluntarily considered by the courts. Thus the de-

¹ See article by him in Goldschmidt's *Zeitschrift für das gesamte Handelsrecht*, "Entwurf des neuen Handelsgesetzbuch," 1896, p. 488.

² *E. g.* Italy, see *infra*, chap. iv, subdiv. 3.

³ "In these days the most useful function of our courts should be to control business within just and honest bounds." Untermeyer, *Some Needed Legislative Reforms in Corporate Management*, Address delivered before the New York County Bar Association (1911), p. 15.

termination of the reasonableness of rates, or prices, and the fairness of competition, both of which questions involve also, indirectly, the question of a fair return upon capital invested, represent functions similar to that which courts would be compelled to exercise in determining whether the capital stock has been fairly paid up by contributions of property other than money.

To insure formal and substantial compliance with the law in the organization of corporations, German legislation has created a control independent of the organizers, initial officers and stockholders; but it has not imposed this duty upon the courts. At most, the court has the duty of appointing the auditors, in default of their appointment by the board of trade. The German law thus wisely leaves to independent business men, through their disinterested appointees, the verification of the various steps of organization.

We have seen that the French system places great reliance upon the remedy of nullification for insuring compliance with the requirements of the law. We have already called attention to the fact that this often operates to the injury of stockholders and creditors rather than to their benefit. German law has not entirely eliminated the action of nullification; it may be instituted by any stockholder, director, or supervisor, if the articles, as recorded, are defective.¹ But an error in the articles, unless it relate to the amount of the capital, or of the par value of the shares, may be cured by amending the articles.² Though the German law is much less stringent in this respect than the French, it is difficult to see where any real interest is neglected.

The German Code appears needlessly harsh in denying to subscribers the right to transfer their interests prior to

¹ Comm. C., sec. 309.

² *Ibid.*, sec. 310.

the registration of the corporation. The codes of the Latin countries make all intermediate holders responsible, in addition to the original subscriber; thus added security is given for the collection of the original subscription. Authority in Germany is divided as to the wisdom of the German provision.¹ Its sole advantage appears to be that of limiting the number of interested parties, during the period preceding complete organization, to those who may be supposed to have some knowledge of the enterprise.

Finally, it is noteworthy that the German law of corporations closely follows the actual conditions of the business world. Business experts assisted in modeling the drafts of the Commercial Code and thus a practical trend, often lacking in other systems, has been given to it. The recognition given to boards of trade and their auditors, the appreciation of the important part played by bankers and brokers in the flotation of shares and by stock exchanges in providing a ready market, all testify to the fact that the legislature has attempted to deal with the corporation as an important factor in the social and economic evolution of the nation and not merely as a legal phenomenon. As Ihering has expressed it, the association type is to be recognized not merely as an isolated relationship arising out of contract, but as an underlying form subserving the purposes of human existence.²

3. ITALY

Legislative Development.—The French *Code de commerce* constituted the basis of the various provincial legislations of Italy during the first half of the last century, with

¹ Gierke favors it while Lehmann considers it of no practical advantage. Gierke in *Zeitschrift für Handelsrecht*, 1896, p. 488.

² *Op. cit.*, i, p. 222: "nicht bloss um ein einzelnes Vertragsverhältniss sondern um eine Grundform menschlicher Zweckverfolgung . . ."

such modifications as were effected by local special laws and general provincial codes. The kingdom of Sardinia, for example, adopted a general commercial code (*Codice di commercio Albertino*) bearing date December 30th, 1842. Following close upon the creation of the united kingdom of Italy, a commercial code (*Codice di commercio del Regno d'Italia*) was formulated after careful preliminary studies, and became a law June 25th, 1865. In the main it followed the trend of the Sardinian code, which in turn was much affected by Napoleonic precedents.¹ The provisions relating to commercial associations, and particularly to corporations, were found, however, to be inadequate after a few years of practical operation. In June, 1869, Mancini proposed a revision, for which a commission was appointed by administrative decree. The commission reported a *projet* in April, 1872, for revising the code, and later, in 1874, a separate *projet* for commercial associations. The absolute necessity for an adequate law of associations influenced the movement for a new commercial code generally, and in 1876, a new commission was appointed; it reported in 1880, its *projet* was finally approved April 2nd, 1882, and became effective January 1st, 1883.²

Existing Law.—Following the French system, the Italian Code prohibits the typical corporation type (*società anonima*) from using any other than a fanciful title or one descriptive of the enterprise.³ It deviates from the French system and resembles the German, in that it differentiates the methods of organization by simultaneous act of organizers and by successive acts of subscribers.⁴ It differs,

¹ Lehmann, *Das Recht der Aktiengesellschaft*, i, p. 73.

² Bing, *La société anonyme en droit italien* (1887), pp. 32-35.

³ Italian Commercial Code [revised to 1909] art. 77; comp. French Commercial Code, arts. 29, 30, according to which the nature of the enterprise must appear in the title.

⁴ Italian Comm. C., arts. 128, 129.

however, from the German system and resembles the Swiss, in placing the period of registration *after* the first general meeting of stockholders.¹ The Italian system is unique in requiring the execution of articles of subscription as well as of articles of incorporation. The articles of subscription vary according to whether the plan of organization is simultaneous or successive. If the former, one or more public documents must establish the fact that the organizers (*promotori*) have subscribed the entire capital stock.² The existence of conditions demanded by the law must be verified and administrators or agents designated who are entrusted with representation until the first general meeting.³

If the organization be successive, *i. e.* effected by public subscription, the organizers execute a prospectus (*programma*) stating the objects of the corporation, its capital, the principal clauses which are to be embodied in the articles of incorporation and the personal benefits which the organizers are to receive pursuant to the corporate statutes, or from the profits of operation. The prospectus must be filed in the commercial court at the *situs* of the company.⁴ Subscriptions may then be taken, either upon copies of the prospectus, or by some instrument embodying certain essential statements of the proposed corporate statutes. In either case, the subscriptions must be notarially verified.⁵

Each shareholder must pay at least three-tenths of the amount subscribed by him. No stock may be issued for less than par and no new stock may be issued before the original capital has been entirely paid up.⁶ After the entire

¹ Italian Comm. C., art. 91; *cf.* Swiss Code of Obligations, arts. 618, 623.

² Italian Comm. C., art. 128.

³ *Ibid.*, art. 128.

⁵ *Ibid.*, art. 130.

⁴ *Ibid.*, art. 129.

⁶ *Ibid.*, art. 131.

capital stock has been subscribed, the organizers must publish the period determined by them within which payment of the subscriptions must be made. Two weeks thereafter, a first meeting must be convened at which money payments must be recorded and an appraiser appointed to verify payments in kind (*conferite*). It must also adopt the corporate statutes and elect directors (*amministratori*) unless this has already been accomplished by designation in the articles. It also elects the syndics (*sindaci*) and must ratify all agreements providing for particular advantages in favor of the organizers.¹

An interesting provision, protective of minority interests at the first meeting, accords the right to any subscriber to demand delay in order that further information concerning the organization be obtained. If the demand is supported by subscribers representing at least one-quarter of the capital stock, an adjournment not exceeding three days must be granted; if a majority support the demand, a delay of not exceeding one month must be granted; if the demand be supported by at least three-quarters of the capital stock a longer delay may be obtained.² If no adjournment is demanded, the meeting proceeds to the adoption of the articles of incorporation (*atto costitutivo*).³ Differing from the Swiss system but in line with that of Germany, the Code expressly provides that no right in the subscription may be transferred prior to complete organization.⁴

The organizers are liable jointly for all obligations assumed in connection with the organization, even though they may have recourse against the corporation for reim-

¹ Italian Comm. C., art. 132.

² *Ibid.*, art. 135.

³ *Ibid.*, art. 136.

⁴ *Ibid.*, art. 137; comp. Swiss Code of Obligations, art. 636 and German Comm. C., sec. 200.

bursement when it is completely organized; if organization is not effected, they have no recourse against the subscribers.¹ Recourse against the corporation is made dependent upon approval of their acts by the first general meeting.² The organizers are prohibited from obtaining personal advantages by reason of organizing the company, except such as are computed on the net profits resulting from the operation of the company, not to exceed certain percentages mentioned in the Code.³

The Code provides certain minimal requisites for the articles of incorporation.⁴ A noteworthy provision requires that verification of compliance with all the legal requirements shall be made by a judicial body, *viz.*, the civil tribunal at the proposed *situs* of the corporation. The articles must be filed within fifteen days following their adoption in the office of the clerk of the court. The court thereupon deliberates in chambers with the public minister, and, if it determines that full compliance has been made, it issues its decree that a transcript of the articles of incorporation be published with the corporate statutes.⁵ The details are regulated by royal ordinance. Publication is made in an official bulletin relating to stock companies.⁶

The Italian Commercial Code also contains criminal sanctions for its mandatory provisions relating to the organization of corporations, though these are less detailed than those of the German Code.⁷

¹ Italian Comm. C., art. 126.

² *Ibid.*, art. 138.

³ *Ibid.*, art. 127.

⁴ *Ibid.*, art. 89.

⁵ *Ibid.*, art. 91.

⁶ *Ibid.*, art. 95.

⁷ A person who makes false statements in respect of subscriptions obtained, payments made, or persons associated with the company, for the purpose of obtaining subscriptions to its shares, or payments thereon, is guilty of swindling (*la truffa*) and subject to the penalties

Like the German Code, Italian law requires that the organizers remain individually liable for all obligations incurred in the name of the corporation until it has been officially registered and its articles of incorporation have been published; and if this is not done within three months from the general meeting, the subscribers may demand repayment of the amounts paid on their subscriptions.¹

4. SPAIN

Legislative Development.—Notwithstanding the brief duration of the Napoleonic régime, Spanish legislation has been greatly influenced by the French codes. The French *Code de commerce* was the model of the Spanish *Código de comercio* of May 30th, 1829. The classifications and definitions are almost entirely those of the French code, though many of the administrative devices are peculiar to the peninsula. The Code of 1829 in turn formed the basis of the codes of Bolivia, Colombia, Costa Rica and other Latin-American states.²

After much deliberation and delay, a new commercial code was adopted August 22nd, 1885, and went into effect on January 1st, 1886.³ This code still contains the basic law applicable to corporations.⁴ As in the French code, corporations are treated in a subhead under the general divi-

prescribed in the criminal code. Comm. C., art. 246. A person who fails to perform any of the duties imposed upon him by law—*viz.* to file the articles of incorporation or corporate statutes, or modifications of the same, or the monthly report, or the balance sheet in form as provided by law and within the prescribed period—is punishable by a fine of fifty lire for each day in which he remains in default. *Ibid.*, art. 248.

¹ Italian Comm. C., arts. 98, 99.

² Lehmann, *op. cit.*, i, p. 374.

³ Translated into French by Prudhomme, *Code de commerce espagnol*, 1891.

⁴ Arts. 151-169.

sion, "Commercial Associations" (*Compañías Mercantiles*).

A general revision of Spanish law is now in the hands of a commission appointed by royal decree on March 11th, 1910. It is its purpose to revise and amplify the Civil Code, Penal Code, Codes of Civil and Penal Procedure and the organic law of the tribunals. It is possible that the commercial law of the country will also be revised in connection with this movement.¹

Existing Law.—The Spanish Commercial Code contains provisions applicable both to commercial associations in general² and to corporations in particular³ (*compañías anónimas*). It also contains regulations applicable to particular types of corporations, such as credit banks, banks of issue and discount, railroads, warehouses, building-and-loan associations and the like.⁴

A corporation is organized in Spain by registering articles of association at the commercial registry. The articles must contain its corporate regulations and all agreements and conditions by which the rights of its members (two or more)⁵ are to be governed.⁶

The articles (*escritura social*) must state:

1. The name and residence of the members.
2. The name of the corporation.
3. The persons charged with its administration and the method of filling vacancies.
4. The share capital and the value of contributions in kind (*bienes aportados*) or the basis of valuation of the same.

¹ *Annual Bulletin of the Comparative Law Bureau of the American Bar Assoc.*, 1910, p. 201.

² *Comm. C.*, arts. 116-124.

³ *Ibid.*, arts. 151-174.

⁵ *Ibid.*, art. 116.

⁴ *Ibid.*, arts. 175-217.

⁶ *Ibid.*, art. 119.

5. The number of shares constituting the capital.
6. The period within which the balance due on the shares, if any, must be paid, or the designation of the person or persons who have the power to fix the final date.
7. The duration of the corporation.
8. Its purposes.
9. The time and manner of convening and holding the general meeting of stockholders (*junta generale*); the circumstances under which special meetings are to be called and the manner of convening and holding them.
10. The subjects reserved to the general meeting and the manner of computing a majority therein.
11. All agreements and particular conditions which affect the rights of the shareholders.¹

There is no obligation to pay in a certain amount of the capital prior to the registration of the company, but one-half must be paid in before registered shares may be converted into bearer shares.² As in the French law, the original subscribers and all intermediate holders are responsible for payment up to the face value of the shares. If a conversion into bearer shares has been made prior to full payment, the apparent possessors (*los que se muestren como tenedores*) of the shares are alone responsible; if these are unknown, the corporation may annul the shares unpaid for and may issue and deliver new ones to satisfy the unpaid balance; it must then account for any surplus to the owner in default.²

No new series of shares may be issued until the antecedent issues have been wholly paid up, and no purchases

¹ Comm. C., art. 151. The eleventh clause (*supra*) is expressed in facultative form in this article but under art. 119 it would seem to be mandatory—"deberá hacer constar."

² *Ibid.*, art. 164.

of its own shares may be made by a corporation even out of profits, except for the purpose of amortization.¹

If any subscription remains partly unpaid, the corporation has the option of attaching the property of the subscriber for the balance due, or of rescinding the subscription agreement and retaining the amount already paid.²

Contributions in kind must be appraised in the manner provided for in the articles and, in default of any special provision in this respect, by experts chosen by the parties, or by an umpire, should the experts fail to agree.³

5. SWITZERLAND

Legislative Development.—Prior to June 14th, 1881, corporations, as indeed, many other branches of the civil and commercial law of Switzerland, were regulated by cantonal laws, fragmentary in character and differing widely from each other. After a long period of deliberation, a Federal Code of Obligations was enacted pursuant to the Constitution of 1874. This law regulates corporations under a special title (*Actiengesellschaften; sociétés anonymes*).⁴

Swiss law does not recognize the strict separation of commercial as distinguished from civil *transactions*, as in France; nor does it draw a sharp distinction between commercial and civil *persons*, as in Germany. Accordingly, the law of corporations is not treated in a separate body of commercial law. The general provisions of the Civil Code, adopted December 10th, 1907, effective January 1st, 1912, are applicable to corporations wherever appropriate. The Code of Obligations still exists as a separate statute, although a general revision is now pending.

Existing Law.—Under Swiss law, the general meeting

¹ Comm. C., arts. 165, 166.

² *Ibid.*, art. 170.

³ *Ibid.*, art. 172.

⁴ Code of Obligations, arts. 612-677.

of subscribers (*Zeichner*) for organization must be held before registration, after all the stock has been subscribed. The general meeting must adopt a resolution that the capital has been fully subscribed and that twenty per cent has been paid in upon each share. The meeting adopts corporate statutes and elects the board of directors (*Verwaltung*) to serve for the first three years.¹ The managers do not constitute a separate organ of the corporation but derive their powers through delegation from the board of directors.²

Another variation from the German system is found in the permission granted to subscribers to transfer their subscriptions to new holders prior to the constitutive meeting. The new stockholders may vote at this meeting provided a resolution to that effect be adopted. The original subscriber, however, continues liable for his subscription.³

It is unnecessary to enlarge upon the system. In the main it follows that of Germany. Certain important variations from the German system relating to the operation of the company will be noted in a subsequent chapter.⁴

Comment.—The similarity in the laws of Italy, Spain

¹ Swiss Code of Oblig., art. 649, subdiv. 4. Silbernagel points out that the strong control exercised under German law prior to the first general meeting has no equivalent in the provisions of the Swiss law. *Op. cit.*, p. 323.

² Art. 650, subdiv. 2, in which it is provided that the mandate is revocable at all times, subject to the right of the manager to demand redress in damages. It is quite customary to designate one or more members of the board as a managing committee (*Ausschuss*, or *Direktion*). They, not the members of the board, are termed the "Directors".

³ Arts. 636-637; Lehmann, *op. cit.*, i, p. 390; Silbernagel, *op. cit.*, p. 325. Under German law, interim certificates must be nominative, whereas in Switzerland (Code of Oblig., art. 636) and in Austria (Comm. C., art. 222) they may be issued to bearer.

⁴ *Infra*, ch. viii, subdiv. 5.

and Switzerland in the organization of corporations may be ascribed to the fact that the legislation of each of these countries dates from the same period. It is to be noted that in both the Italian and the Swiss system, emphasis is laid upon the first general meeting of subscribers or shareholders. The resolutions and appointments of this first or constitutive meeting form the principal elements of the documents for the registry. This has an advantage, because prospective stockholders and creditors are apprised of the policy of the corporation and the character of its management from the very beginning, whereas in Germany, the corporation may come into existence before the directors and supervisors are elected. The Spanish Code resembles the German in postponing the first general meeting until after registration. The Spanish Code furnishes but slight protection to creditors as it permits the organization of companies with little or no capital actually paid up. No specific percentage of the share capital need be paid prior to registration and even bearer shares may be circulated if one-half of the amount of the capital has been paid. Furthermore, there is no check upon organizers and *apporteurs*; the French legislation of 1867 seems to have had but little influence in Spain.

Italian legislation lays great stress upon the importance of a judicial control over the payment of the capital. In committing this function to the courts, it has gone even beyond the French system, which attempts to accomplish the purpose by placing increased power in the hands of stockholders other than organizers.

The Swiss Code demands acceptance of the corporate statutes *in toto*, with the very act of subscription. The legislative purpose is to prevent any change whatever in the nature of the organization between the period of obtaining subscriptions and the actual consummation of the organi-

zation.¹ In this it is even more stringent than the German law, which requires simply a reference to the essential provisions of the corporate statutes in the subscription agreement.

¹ Silbernagel, *op. cit.*, p. 119.

CHAPTER V

LEGISLATION AND REFORM IN ENGLAND AND AMERICA.— ORGANIZATION

Legislative Development in England.—We have seen that the so-called "Bubble" Act of 1720¹ prohibited the transfer of shares of any unincorporated company; so that unincorporated joint-stock companies, as far as we know, were treated as ordinary partnerships. This condition continued till 1825. By reason of the cessation of the Napoleonic wars, trade had developed anew. The complications and difficulties connected with the grant of a charter from the Crown or Parliament, together with the manifest convenience of the corporate form of association, induced Parliament to repeal the Bubble Act,² which revived the state of law prior to that act. The common law, with its prohibition against the transfer of any shares without the consent of all of the associates, necessitated the insertion of a clause in the articles of association permitting the transfer of shares with the consent of the officers. The shareholders continued, however, to remain liable to an unlimited extent.³

The next step was taken by the statute of 1844,⁴ under

¹ 6 George I, c. 18.

² Cf. Lindley, *On Companies*, p. 3; the repealing statute is 6 George IV, c. 91.

³ See Cunningham, *The Growth of English Industry and Commerce*, *Modern Times*, part i, p. 279; Lehmann, *op. cit.*, p. 84.

⁴ 7 & 8 Vict., c. 110.

which associations consisting of more than seven members might become invested with corporate entity by fulfilling certain conditions and registering the by-laws and other particulars. The statute did not permit the issue of shares payable to bearer nor did it provide for a limited liability; practically, therefore, it accorded only the right to sue and be sued under the corporate name.

In 1855, the Limited Liability Act¹ provided for limited companies with shares of a par value of at least ten pounds. This was followed in the two succeeding years by statutes extending the privilege of limited liability to all companies except certain classes mentioned, such as banking and insurance companies.²

The concessionary system was abandoned from 1844 onwards, but it was not until 1862 that a complete system of incorporation and control was enacted, in the form of a consolidation and revision of all prior acts.³ The statute was practically a code of company law and regulated the three classes of companies recognized in English law, *vis*: (1) the unlimited company having a capital divided into shares, (2) the company limited by guaranty and having a capital divided into shares, and (3) the company limited by shares. It prohibited bearer shares; but the statute of 1867⁴ permitted the issuance of "share warrants" to bearer.

Frequent amendments, additions and revisions of the Companies Act of 1862 have been made since that time, detailed reference to which is unnecessary. It is sufficient to say that in 1900, under the form of an act amending that of 1862, an entirely new system of company law was

¹ 18 & 19 Vict., c. 133.

² 19 & 20 Vict., c. 47; 21 Vict., c. 17.

³ 25 & 26 Vict., c. 29.

⁴ 30 & 31 Vict., c. 131.

introduced. This was made necessary by the abuses which had arisen in connection with the large number of companies launched for exploitation in the colonies. A rigorous regulation of the company prospectus was made one of the principal features of English legislation.¹ The statute of 1900 was the result of patient research, originally carried on by a private commission, afterward by a committee of Parliament itself.² It represented one step in a progressive legislative policy primarily concerned with the protection of creditor and stockholder and culminating in the consolidated statute of 1908 known as the "Companies (Consolidation) Act, 1908."³

Legislative Development in America.—After the Revolution, the states succeeded to the power of the Crown to grant charters of incorporation. The old concessionary system continued uninterruptedly until 1837, when Connecticut passed the first general act of incorporation for business companies. Corporations could be organized under the statute for purposes limited to those necessary or proper for the accomplishment of a single object; the corporation was given a lien on the stock of its members for debts due to it; and the stockholders were personally liable for all capital refunded or dividends illegally declared.⁴

By 1850, about twenty states had passed general incorporation statutes, modeled more or less closely on the Connecticut act. This legislation proved so satisfactory that constitutional prohibitions against the creation of business corporations by special act of the legislature were adopted

¹ See Segnitz, *Prospectus dans les sociétés anglaises par actions* (1908), p. 8.

² *Ibid.*, p. 32.

³ 8 Edw. VII, c. 69.

⁴ Frost, *A Treatise on the Incorporation and Organization of Corporations* (1908), p. 2.

in most of the states. This right is now reserved to the legislature in only six states, all of them being of the original thirteen.¹

The next development was toward the enlargement of the corporate purposes and powers permitted by the articles. Statutes were passed granting the right to do business outside the state, to hold stock in other corporations, even when not directly necessary to the immediate purpose of the holding corporation, and to amend the charter in any manner lawful for an original incorporation. The taxes derived from corporations both at the time of incorporating and during their operation became a considerable item in the revenue of the states. Therefore a sort of competition grew up among them in devising and passing "liberal" incorporation laws, thus inducing corporators to take advantage of their benefits.²

During the past two decades, abuses of the greater liberality of corporate statutes have been frequent. This, together with the tendency of our industrial system toward centralization and combination, has influenced public opinion in favor of a stricter control of business corporations. The important revenue derived by the states from corporations organized under local authority continues to be a real obstacle in the way of progress. The states have begun to feel the concurrent taxing powers of the Federal Government, and therefore few of them are willing to enact stricter corporation laws which might cause the loss of revenue from a source at present both important and certain. Initiative in reform is therefore to be sought from the Federal Government, with its power of control over interstate commerce.

¹ Horack, *op. cit.*, p. 26 n.

² This applies particularly to laws of Delaware, Maine, New Jersey, New York, and West Virginia. Frost, *ibid.*, pp. 2-3.

Existing Law and Reforms.—England has partially returned to the legislative policy of the Bubble Act of 1720, directed against the association of large numbers of persons without corporate form. It is recognized that the corporation, when properly regulated and controlled, is more easily held under governmental supervision and restraint than unincorporated aggregations of individuals; accordingly, associations or partnerships of more than twenty persons are prohibited.¹

English law still retains the classification introduced in 1862, *viz.* companies limited by shares, which are the ordinary business companies known to the laws of the American states; companies limited by guaranty, in which the liability of the members is limited in the articles to such amount as the members may undertake to contribute to the assets of the company in the event of its being wound up; and unlimited companies. In a company of the first or second type, the memorandum of association must state the name of the company with "Limited" as the last word of its name.

Corporate Title.—The requirement of some designation to show the limited character of the company is doubtless intended as a protection to prospective creditors. The attitude of legislatures in America would, however, seem to indicate a difference of opinion as to the importance of this feature, many states permitting the use of a corporate title similar to that of an individual or partnership.² On the other hand, many other states require that the name

¹ Companies (Consolidation) Act, 1908, sec. 1, (2).

² Ark. Dig. of Stats., 1904, sec. 855; Cal. Code, 1907, sec. 290; Ga. Code, 1910, sec. 2822; Ill. Gen. Corp. L., sec. 2; Ind. Burns Stats., 1908, secs. 4286, 5062; Me. R. S., c. 47, sec. 7 (1907); Mich. Corp. Act, 1903, sec. 2, par. 1; N. J. Corp. Act, as amended to 1910, sec. 45; N. Y. Gen. Corp. Law, as amended to 1911, sec. 6; Penn. Corp. Act, 1874, sec. 3.

shall indicate that the association has been incorporated, either by commencing with the word "The" and ending with the word "Company" or "Corporation," or by placing the word "Incorporated" or "Limited" immediately after the name, or by some other form of designation.¹ The Commissioners of Uniform State Laws, in their draft bill for a uniform law of incorporation,² propose that the name shall "be such as to indicate that it is a corporation, as distinguished from a natural person or partnership." A business might thus be continued under an old individual or partnership title by simply adding the letters "Inc.," to the old title. This would permit the good-will to be preserved and seems sufficient for all purposes.³

The manner in which the memorandum or certificate of incorporation shall be executed is a matter of form, rather than of substance, and does not affect the interests of stockholders or creditors. The *content* of the certificate, however, is of great importance, for it is in legislating upon what the certificate shall contain that the statutes usually regulate the amount of the capital stock and the proportion which must be subscribed for prior to filing the certificate.

The English Act simply requires that the memorandum

¹ Ala. Code, 1907, sec. 3447; Conn. Pub. Acts, 1907, c. 155; Ky. Stats., 1909, sec. 2161 (it need not be a part of the name but must appear on all signs and on printed and advertising matter, under penalty of fine); Mass. Bus. Corp. L., sec. 5; Md. Rev. Corp. Act, 1908; Minn. R. L., 1905; sec. 2849; R. I. Gen. Laws, 1909, c. 212, sec. 9; Wis. Sanborn's Stats., sec. 1772, as amended by L. 1911, c. 341.

² Second Tentative Draft of an Act to Make Uniform the Law of Incorporation of Business Corporations, July, 1911, p. 14.

³ The bill introduced (1910), under the auspices of the national administration, for federal incorporation of interstate or international business, provides that the words "national incorporation" shall be the last words of the name. The name itself must be approved by the Commissioner of Corporations. Senate Bill, no. 6186, 61st Cong., 2nd session, sec. 2.

shall state the name of the company, the part of the United Kingdom in which the office is to be situated, the objects of the company, the limited liability of the members, the amount of share capital and the number of shares which each subscriber takes.¹

Capitalization.—Legislation in the United States generally requires a minimum amount of capital with which a corporation may commence business, but it is interesting to note that a few states also fix a maximum limit of capitalization.²

The provision seems to have found favor with the Commissioners of Uniform State Laws, for in their draft a minimum and maximum limit are provided for, although the amounts are not stated.³ We have seen that no limitation of such a character exists in any Continental European statute, nor does it exist in England. The amount of the capitalization has no direct bearing on protection to stockholder or creditor, and the considerations in its favor would seem to be of a political rather than legal character.

No limitation of the *par value* of the shares is contained in the English statute, and the same is true in most of our states. A number, however, have placed a minimum limit on the *par value* of shares to be issued.⁴ The Com-

¹ Companies Act, 1908, sec. 3.

² Mich. \$25,000,000; Corp. Act, 1903, sec. 2, par. 1. N. H. \$5,000,000; L. of 1907, c. 129. Pa. \$1,000,000 except manufacturing or mining corporations which may be incorporated with a capital not exceeding \$5,000,000 and thereafter increased to any amount; Corp. Act, 1874, sec. 39; L. 1889, p. 180; L. 1905, p. 280, sec. 1. Vt. \$10,000,000 unless a judge of the Supreme Court shall determine that there is no monopoly or restraint of trade; Pub. Stats., 1906, sec. 4311, amended L. 1910, no. 143, sec. 4.

³ Second Tentative Draft, p. 14.

⁴ Conn. \$25; Pub. Acts, 1903, c. 194, sec. 63. Mich. \$10; Corp. Act, 1903, sec. 2, par. 5. Mass. \$5; Bus. Corp. L., 1903, sec. 8. N. Y. \$5; Bus. Corp. Law, 1910, sec. 2.

missioners of Uniform State Law have proposed that the par value shall not be less than \$10 nor more than \$100.¹ A provision for a higher minimum might well be protective of small investors inclined to make investments of reckless character merely because the denomination of the shares accords with the limited amount of funds at their disposal. The German statute has adopted a high denomination (\$50 approximately) with the object of discouraging speculation in wildcat ventures and the exploitation of that part of the public least able to bear the loss.

Publicity of Personnel.—It is, of course, of great importance at the time of organization that prospective creditors and stockholders be apprised by some public record of the fiduciaries who are to manage the corporation.²

Contrary to the system of most of the countries of Continental Europe, as well as many of the American states, English law does not require that the memorandum shall state the names of the directors for the first year. It is true, a consent signed by the persons who are willing to be directors must be filed with the registrar on registering the memorandum; but these persons are not necessarily the directors actually elected for the first year.³ The "articles of association" in England, which embody the "regulations" (corresponding to the "by-laws" of corporations organized in the United States), usually contain some provision with regard to the number and qualifications of directors and a statement of the names of the directors for the first year. The adoption of articles for a company limited by shares is, however, merely optional.⁴ The act

¹ Second Tentative Draft, sec. 2, iv.

² See Horack, *The Organization and Control of Industrial Corporations*, p. 61.

³ Companies Act, 1908, sec. 72.

⁴ *Ibid.*, sec. 10, subdiv. 2.

contains a schedule of standard forms of articles and in the event that no other articles are adopted and registered, or if the articles as registered do not exclude or modify the regulations in the schedule, it is declared that the latter shall be deemed the regulations of the company so far as applicable.¹ The schedule provides that the first directors shall be designated in writing by a majority of the subscribers to the memorandum of association.² Every company must keep at its registered office a register of the names, addresses and occupations of its directors and managers; it must send a copy to the registrar and notify him of any changes.³

In most of our states, the names and addresses of the first directors must be inserted in the certificate of incorporation.⁴

Although the matter, perhaps, lies outside the scope of the present chapter, it is of equal importance that the names and addresses of directors subsequently elected should also be subjected to publicity. The New York law approaches but does not accomplish this purpose. The oath of the inspectors of election, together with a certificate of the result of the vote, must be immediately filed in the office of the clerk of the county in which the

¹ Companies Act, 1908, sec. 11.

² *Ibid.*, First Schedule, Table A, sec. 68.

³ *Ibid.*, sec. 75.

⁴ Cal. Code, sec. 290, amended 1907; Col. R. S., 1908, sec. 847; Ind. Burns Ann. Stats., 1908, sec. 5062; Minn. R. L., 1905, sec. 2849; N. Y. Bus. Corp. L., 1910, sec. 2, subdiv. 2; Wis. Sandborn's Stats., 1911, sec. 1775 b. Many states leave the number to be determined by the by-laws and the election takes place at the first meeting of shareholders. Conn. Pub. Acts, 1903, ch. 194, sec. 193; Ga. Code, 1910, sec. 2822; Ill. Gen. Corp. L., sec. 2; N. J. Corp. Act, rev. to 1910, sec. 8; Ohio. Gen. Code, 1910, sec. 8625; see also Second Tentative Draft of Comms. of Uniform State Laws, p. 16, n. 7.

meeting is held. But there is no penalty imposed, or other sanction created, for the enforcement of this provision, and it therefore remains practically unobserved.¹ The preferable system is to compel, under penalty, the filing of an annual report containing the names and addresses of officers and directors for the ensuing year.² We have seen that in Germany and in other Continental European countries, any change in directorate or management, from whatever cause, must be promptly filed at the commercial registry.

Subscription to and Payment of Capital Stock.—Probably the most important feature of organization affecting creditors and stockholders relates to the subscription to and payment of the capital stock. Professor Burgess has said that "when the government confers upon a number of people, uniting themselves in corporate capacity, the privilege of limited liability, sound political science ascribes to the government the duty of seeing that the capital stock is all paid in and that it remains corporate property."³

The corporation should not operate until a sufficiently large amount of stock has been subscribed to insure a degree of economic strength bearing some relation to the amount of its authorized capital.

Under English law, the organizers fix the minimum subscription upon which the directors may proceed to allotment; and no allotment may be made until payment of the sum payable on application for the amount so fixed.⁴ The

¹ N. Y. Stock Corp. Law, rev. 1911, sec. 31; White, *On Corporations*, 1909, pp. 270-271.

² Ind. Burns Ann. Stats., 1908, sec. 4080; N. J. Corp. Act, rev. 1910, sec. 43.

³ "Private Corporations from the Point of View of Political Science", in *Pol. Sci. Quar.* (1908), xiii, p. 205.

⁴ Companies Act, 1908, sec. 85.

amount payable on application must not be less than five per cent of the par value. The company may not begin any business, or exercise any borrowing powers, unless the shares allotted and subscribed for amount to not less than the minimum subscription; furthermore, every director must have paid on the shares subscribed for by him a proportion equal to that payable on the application and allotment of shares to the public. In most of the American states, on the other hand, corporations are permitted to begin business (and incur debts) although only an insignificant proportion of the capital stock has been subscribed. Thus New York requires no more than \$500, payable in money or property.¹ Delaware and New Jersey require \$1,000, which must be subscribed, but not necessarily paid for.² West Virginia requires ten per cent of the shares subscribed to be paid at the time of subscription, but does not require any fixed proportion of the capital stock to be subscribed, so that, apparently, a payment of ten per cent on one share will authorize the commencement of business.³ Georgia, Michigan and Pennsylvania require ten per cent of the authorized capital to be paid in.⁴ Many of the states have no provision whatever as to the amount of subscription or payment required before the corporation is authorized to do business. The result of this lack of statutory protection to creditors is that a corporation capitalized for a huge amount may begin operations with but a few shareholders, and but a paltry sum, or perhaps nothing at all, in its treasury. The dan-

¹ Bus. Corp. L., secs. 2-3.

² Del. G. Corp. L., sec. 5; N. J. Corp. Act, sec. 8.

³ Code, 1906, c. 53, sec. 25.

⁴ Ga. Code, 1910, sec. 2822; Mich. Corp. Act, 1900, sec. 2, par. 6; Penn. Act of 1874, sec. 39, par. 3.

ger which a corporation organized under such auspices may cause to the community, especially when in the hands of unscrupulous promoters, cannot be overestimated.

In order to prevent this evil, some of the states have provided that a certain percentage of the capital stock shall be subscribed *before* the certificate is filed, twenty-five per cent in Alabama,¹ fifty per cent in South Carolina² and Michigan.³ Wisconsin⁴ requires that fifty per cent be subscribed for and twenty per cent paid in before the corporation may begin business; Illinois,⁵ that the stock be fully subscribed.

The Commissioners of Uniform State Laws, in their draft act, have provided that fifty per cent of the capital must be subscribed before the filing of the certificate; that the corporation shall not begin business or incur debts until twenty-five per cent of the authorized capital shall have been paid in; and that seventy-five per cent of the capital stock must be paid in within one year, or the corporation shall be *ipso facto* dissolved.⁶ The provision for dissolution, like the similar provisions of the French law with regard to "nullification" of corporations,⁷ is of doubtful value, as it paves the way for injury to innocent parties. A provision permitting dissolution, if the proportionate amount has not been paid in within one year, is found in the New York law. The power given to the attorney-

¹ Code, 1907, sec. 3447.

² Civ. Code, 1902, sec. 1884.

³ Corp. Act as amended by Act 146 of 1907, sec. 2.

⁴ L. 1905, p. 940.

⁵ Gen. Corp. L., sec. 4.

⁶ Second Tentative Draft, sec. 1, subdiv. 3, sec. 8.

⁷ See *supra*, chap. iv, subdiv. 1.

general to bring the proceedings has, in practice, operated as a sufficient sanction for this provision.¹

Overcapitalization.—The overcapitalization of corporations has ever been one of the chief sources of evil resulting from the corporate form. All countries in which corporations have played a large part in commerce and finance have suffered at times from the effects of overcapitalized securities. It is obvious that the same danger to the stability of the financial community as a whole may result from a prevalent condition of overcapitalization, as though all corporations were permitted to extend their credit obligations unreasonably beyond the amount of their net resources. The difference lies simply in the fact that in the one instance the crisis is apt to come sooner, because the creditor may demand the sum due him within a limited period of time, whereas the stockholder liquidates his investment by transferring the evidence of it to another. Thus the day of reckoning is postponed, but the last purchaser suffers most of the loss. The danger to society through the collapse of the market values of securities in a period of great depression is too widely appreciated to require further mention.

To prevent overcapitalization, many devices have been proposed. Among these is a general limitation upon the amount of capital stock which corporations may be authorized to issue. We have seen that a number of states have enacted maximum limitations. It is plain, however, that the mere limitation of capitalization is not a corrective; a corporation capitalized at a moderate figure may be proportionately more inflated than one capitalized beyond the maximum. The bill for federal incorporation does not provide for any limitation upon the capital, nor is there any in England or in Continental European countries.

¹ Business Corp. Law, sec. 5. White, *On Corporations*, 1909, pp. 367-369.

If, as was said after the Civil War, the best way to resume is to resume, the best way to prevent overcapitalization is to prohibit the issue of capital stock in excess of the actual market value of the resources supporting such capital stock.

The English Act does not *directly* attempt to prevent overcapitalization. It assumes to correct the evils of overcapitalization by insisting that the consideration in payment of the subscription, if not in money, shall be publicly revealed in a prospectus or statement equivalent to a prospectus. The prospectus, if issued, besides stating the facts relating to founders, directors, subscribers, division of the shares, minimum aggregate subscription, *etc.*, must also give the names and addresses of the vendors of any property proposed to be acquired by the company, either out of the proceeds of the issue of the shares or in exchange for shares or debentures, specifying the amount, if any, payable for good will, also the amount paid for underwriting and to promoters, the estimated amount of preliminary expenses and the nature and extent of the interest of every director in the promotion of the company or in the property proposed to be acquired.¹ A company which does not issue a prospectus must file with the registrar in lieu of a prospectus a statement embodying practically the same information, signed by every director or proposed director.² A direct liability for compensation to all persons who subscribe for shares or debentures on the faith of a prospectus is imposed upon every director or promoter and every person who has authorized the issue of the prospectus.³ This covers loss or damage

¹ Companies Act, 1908, secs. 80, 81.

² *Ibid.*, sec. 62.

³ According to English law and the laws of the American states, the

sustained by reason of any untrue statement therein, unless it be proved that there were reasonable grounds for believing it to be true and that the defendant believed it to be true up to the time of the allotment of the shares or debentures.

Though English law is thus much in advance of prevailing legislation in most of the American states, it still permits wide latitude in the organization of companies partly or wholly capitalized upon the value of property transferred, insisting only that the disclosure of pertinent facts be full and truthful. In this respect, it fails to give stockholders and creditors the degree of protection that is afforded by Continental European law, particularly by that of Germany and Italy, where an independent body is charged with the duty of valuing the *apports*, and untrue statements are visited with criminal penalties.

Certain of our states have indeed made an attempt to control overcapitalization by prohibitive clauses, more or less general, contained both in constitutions and statutes. The constitution of Delaware provides that "no corporation shall issue stock, except for money paid, labor done, or personal property, or real estate or leases thereof actually acquired by such corporation."¹ Notwithstanding this clause, the statute² makes the judgment of the directors decisive, in the absence of fraud, as to the value of such labor or property. A similar provision exists in New Jer-

term "organizers" is not technical. In English law the term "promoters" is made use of more frequently than in the United States, where it has obtained a popular rather than definite signification. Lindley defines the class as: "those persons who bring the company into existence, *i. e.* by taking an active part in forming it or in procuring persons to join it as soon as it is technically formed." (i, p. 481.)

¹ Art. ix, sec. 3.

² Act of 1901, sec. 14.

sey.¹ We also find expressions such as the following: property may be received in payment of stock "to the amount of the value thereof";² "actual value";³ "at its true money value";⁴ cash, or "land at a fair cash value";⁵ "at a just valuation to be fixed by the corporators, or by the directors";⁶ "the valuation placed by the stockholders" is, in the absence of fraud, "binding upon any and all creditors of the corporation."⁷

All of these devices, however well-intentioned, must prove abortive unless some administrative body exercises a power of control in execution of the statute. Usually a breach of the plain provisions of the statute will give rise only to an action at law brought on behalf of the creditors, acting vicariously through a receiver, against the original subscribers or ultimate holders of shares. The gravamen of such an action must necessarily be that the assessment or call has not been fully paid. It is frequently directed against innocent purchasers of the shares. The statutes furnish no protection to shareholders who have fully paid for their subscription in money.

In some states, the beginning of an administrative control over the transfer of property in payment of shares is discernible. Thus, in Iowa, the executive council of the state is created an official appraiser.⁸ In Rhode Island, under certain circumstances, the tax appraisers of the town

¹ Law of 1896, revised to 1911, sec. 49.

² Penn. Act of 1874, sec. 17.

³ Conn. Pub. Acts, 1903, c. 194, sec. 12.

⁴ N. D. Code, 1905, sec. 4195.

⁵ Tenn. Code, 1903, sec. 2335.

⁶ Fla. Gen. Stats., sec. 2653.

⁷ Md. Rev. Corp. Act, 1908, sec. 36.

⁸ 32 Gen. Acts, c. 71, secs. 1-3; 34 Gen. Acts, c. 76, sec. 1.

wherein a manufacturing company is situated act as appraisers of property purchased for stock.¹

The variance in legislation is ascribable to a variance of legislative policy. During the period after the Civil War, great inducements were offered to encourage investments in constructive enterprises. It was deemed desirable to permit overcapitalization, in order that corporations might "grow up" to the valuation artificially placed upon their resources. This is probably still the legislative policy in England, with its many ambitious schemes of colonial expansion and exploitation. It probably continues to be the policy of most of our states. But with the advance in the development of the country, capital has shown an increasing tendency to concentrate, and with greater abundance of capital the original motive for liberality in respect of capitalization has largely disappeared.

The proposed bill for federal incorporation has dealt with the subject in a thoroughgoing manner. It provides that while the board of directors may issue stock for property purchased to the amount of the value as fixed by them, every certificate of stock so issued shall contain a statement

¹ Gen. Laws, 1909, c. 214, sec. 8. The Commissioners of Uniform State Laws in their draft act propose the following solution: Second Tentative Draft, sec. 3: "Where subscriptions to the capital stock of a corporation organized under this act shall consist in whole or in part of property, there must appear in the articles of incorporation a description thereof, together with a statement of its fair cash value, as appraised by the directors, supplemented by affidavits of at least three disinterested persons, that they are acquainted with the said property, that they have personally examined the same, or in such other manner as may be authorized by law, and that it is reasonably worth the amount in cash for which the incorporators have accepted it; if made subsequent to incorporation, a similar description and appraisement must be filed in the office of the (secretary of state) and in the office of the (county clerk) wherein the principal place of business is located within ten days after the subscription is approved. Stock so issued shall, in the absence of fraud, be full paid stock."

that it was issued for property purchased and the stock must be so reported in subsequent reports. It is further required that a statement, signed and sworn to by a majority of the board of directors, be filed with the bureau of corporations before such stock is issued, giving a full description of the number of shares to be issued, the names and addresses of the vendors and whether they are officers or directors of the company and owners of any of its shares of stock, the terms of agreement for the transfer of property (including the amount payable for good will), and, if the vendors are directors of the corporation or owners of any of its stock, a statement of the prices originally paid by them for the property.¹

The plan seems to have been taken from the provision of the English statute relating to the prospectus. In addition, an attempt has been made to secure an official valuation by the commissioner of corporations, whenever the shares of stock have a par value. An appraisalment of the value of the property by two disinterested appraisers must be filed and approved in writing by the commissioner; he may appoint one or more other appraisers to value the property at the expense of the corporation, and no stock may be issued in payment of property to an amount in excess of the value as approved by the commissioner after such appraisalment.² The approval of the commissioner of the value of property shall be conclusive as against the corporation and its stockholders and creditors. This does not absolve the directors for damage caused by a false statement to subscribers, holders and purchasers of the stock issued; and the burden is thrown upon the defendants to show that the shareholder or creditor had no knowledge of and did not rely upon the statement.³

¹ Senate Bill, no. 6186, 61st Cong., 2nd session, sec. 17.

² *Ibid.*, sec. 17, f.

³ *Ibid.*, sec. 17, g.

The bill, therefore, unites the features of the English statute, so far as relates to disclosure of details in connection with the purchase of property, with that of the Iowa statute in regard to an administrative valuation, and it adopts the German feature of a direct joint and several liability of the directors or supervisors to an injured stockholder or creditor.

One of the devices suggested in recent years to avoid overcapitalization is that of issuing stock in aliquot parts without a par value. It is assumed that when the par value disappears, the fictitious value thus given to the share will also disappear. The federal incorporation bill provides optionally throughout for shares of capital stock without par value. A recent amendment to New York laws is also designed to encourage the issuance of this type of shares.¹ A general adoption in practice (which does not seem likely) would bring us back to the joint-stock type of the 16th, 17th and 18th centuries. Historical experience teaches that the aliquot shares attained values as fictitious as those often found at the present time, producing all of the evils attending overcapitalization. By depriving the divisional parts of a nominal value we do not cure the evil of the overcapitalization of the whole. Only the most ignorant will assume that the par value of a share of stock must necessarily be its real value. The par value is simply a convenient fraction into which the share capital has been divided. A decimal system of currency is more convenient than one based upon the actual value of various units of gold or other precious metal. If the same evils were permitted in respect of a capitalization without par value as exist at the present time, the creditor and stockholder would be no better off in respect of security. The incidents of an evil are often mistaken for its cause. What is required is an effective control over organization and administration; not a mere change in the association type.

¹N. Y. Laws of 1912, ch. 351.

CHAPTER VI

PROTECTION OF CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE.—OPERATION

I. FRANCE

Existing Law.—The Commercial Code in its original form contained only a few rules in respect of the management of corporations. It provided that corporations should be administered by mandataries serving for a limited period. They might or might not be shareholders and were to serve with or without compensation, under a revocable mandate. They were made responsible for the execution of the mandate, but in contracting in the name of the corporation they were not to incur any liability.¹

The Law of 1867 created three organs of corporate management, *viz.*, the directors (*administrateurs*), the general meeting of stockholders (*assemblée générale*), and the auditors (*commissaires*). The first general meeting elects the directors and auditors for the first year, or for a period not exceeding six years, and both classes are eligible for re-election.² The directors constitute a board of management but, as a rule, delegate the actual management of the business to a committee of one or more of their own number. If the corporate statutes specifically so per-

¹ Comm. C., arts. 31, 32. Art. 31 has been incorporated into art. 22 of the L. of 1867; art. 32 retains its position.

² L. of 1867, art. 25.

mit, the management may be delegated to one or more *not* members of the board.¹

All of the directors must be stockholders and must deposit a certain number of shares, fixed by the articles of association, as a guaranty for their acts as managers.² The directors may not be interested directly or indirectly in any undertaking or agreement made on behalf of the corporation, unless specially authorized by the general meeting. In the event that the general meeting authorizes a transaction in which any director is interested, a report must be made in regard to the transaction and agreements finally entered into.³

For breach of the fiduciary obligations of a director, the law provides for either an individual or a joint and several liability, as the case may be, according to whether the act was performed with or without the concurrence of other directors.⁴ As they are declared to be mandataries, it follows that the provisions of the Civil Code apply. They are therefore held responsible not only for fraud (*dol*), but also for errors (*fautes*) committed by them as such; except that mandataries serving without compensation are subjected to a less rigorous test of responsibility than those who are compensated.⁵

¹ L. of 1867, art. 22. Goirand says: "This measure has been considered expedient in order that the society may benefit by the services of a person possessing the necessary special technical requirements, even though such person be not possessed of the number of shares required by law." *French Commercial Law and Practice of the Courts*, 2nd ed., p. 81.

² L. of 1867, art. 26. The original *Code de commerce* permitted the directors to be chosen *dehors*; cf. art. 31.

³ *Ibid.*, art. 40.

⁴ *Ibid.*, art. 44. Court of Appeal, Paris, August 1st, 1868. See also Lyon-Caen and Renault, *Manuel de dr. comm.*, p. 208.

⁵ Civ. C., art. 1992.

As the general meeting determines whether an action shall be instituted against a director, the protection accorded the shareholder, especially a minority shareholder, is much less effective than under the law of Germany.¹ The shareholder has no right to institute the proceedings either in his own name, nor in the name of the corporation, until after ratification by the general meeting.²

The law does not specifically make the directors responsible to creditors for illegal acts, such as depleting the funds of the corporation through the payment of unearned dividends, yet the courts find no difficulty in awarding damages to creditors, or third parties generally, who have suffered special damage by reason of the illegal act of a director.³

A salutary check upon the board of directors has been instituted by the Law of 1867, in its provision that no resolution of the general meeting approving the balance sheet and accounts shall be valid unless preceded by a report of the auditors.⁴ The annual general meeting appoints the auditors who are charged with the making of the report for the ensuing year. In default of their appointment by the general meeting, any person interested may request that they be appointed, after due notice to the directors, by the president of the tribunal of commerce at the *situs* of the corporation.⁵

During the three months which precede the date fixed by the articles for convening the general meeting, the audi-

¹ *Infra*, chap. vi, subdiv. 2.

² Court of Appeal, Paris, April 16th, 1870; Dalloz, *Recueil periodique*, 1870, part 2, p. 121.

³ Court of Cassation, May 7th, 1872; Dalloz, *ibid.*, 1872, part 1, p. 233

⁴ L. of 1867, art. 32.

⁵ *Ibid.*

tors have free access to the books and records of the corporation. They may convene the general meeting at any time and are responsible to the shareholders for negligence in the performance of their duties.¹ It is the duty of the directors to prepare an annual inventory and a profit-and-loss account, and to place it at the disposal of the auditors. They must create out of the net profits a reserve fund, equal annually to at least one-twentieth of the net profits; but this amortization ceases to be obligatory when the reserve reaches one-twentieth of the capital stock.²

In the event of loss of three-quarters of the share capital, the directors must convene the general meeting of shareholders, in order to determine whether the corporation shall be dissolved, in default of which any person interested may demand the dissolution of the corporation in the courts.³ It has been held that if the insolvency of the corporation is due to the wrongful act of its directors, two classes of action are open to stockholders or creditors. The one must be instituted in a corporate capacity (*action sociale*) against the director, as a mandatary under the provision of articles 1991 and 1992 of the Civil Code; the other is individual (*action individuelle*) by reason of the provisions of articles 1382 and 1383 of the Civil Code. These are framed in general terms and create a liability against all persons who have caused injury to another by their fault, negligence or imprudence.⁴

Thus, for example, a person who had been induced to become a stockholder by publication of a false prospectus, or balance sheet, would have a right of action in his individual capacity, even though the defendant were not guilty

¹ L. of 1867, art. 33.

² *Ibid.*, arts. 34 and 36.

³ *Ibid.*, art. 37.

⁴ Court of Appeal, Rennes, August 1st, 1900, Dalloz, *ibid.*, 1901, part 2, p. 300.

of a breach of duty toward the corporation. On the other hand, the remedy of a shareholder or creditor for injury to his security by reason of a declaration of unearned dividends would necessarily be by action brought in the name of the corporation, because arising out of the breach of the director's mandate.¹

In order that the shareholder may not be put to inordinate expense in protecting his rights against the directors or managing committee, a special exception has been made in the law of corporations to the French rule of procedure that actions must be brought by the real party in interest. Accordingly, stockholders who represent at least one-twentieth of the share capital may appoint a mandatar to represent the interests of all before the court.²

Comment.—The system of administration and control devised by the legislation of 1867 was doubtless far in advance of any other Continental European system prior to that time. Even the German Commercial Code of the present day has retained many of its features. Experience teaches, however, that the French system of a single organ of management, *viz.*, the board of directors, is inferior to a bi-organic control, each organ acting independently, with separate powers and responsibilities. The board of directors of a business company may contain men of large experience, yet with small opportunity for obtaining precise information in regard to the affairs of the corporation over which they have control. This is usually left to one, or a few, who thus exercise practically the entire power of the board. It has been said that

¹ Silbernagel, *op. cit.*, p. 425; Lyon-Caen and Renault, *Manuel de dr. comm.*, pp. 207-208.

² L. of 1867, arts. 17, 39; Vavasseur, *Traité des sociétés civiles et commerciales* (1897-1904), ii, pp. 400, 403; Lyon-Caen and Renault, *Traité du droit commercial*, ii, p. 710.

"the principal defect of corporations (under the French system) is that they are without control, either from within or without."¹ It is true that the law provides control by the auditors; but this applies only to the period immediately preceding the annual meeting, and many errors may be committed in the interim periods. Furthermore, the auditors are designated by the same majority which appoints the directors themselves. Indeed, it would seem to be the practice in France to consider the auditor as a candidate for future election to the directorate; accordingly, he is not desirous of incurring the enmity of those who may be influential in obtaining his election.² Unless the auditors are exceedingly well paid, which is not often the case, they have no incentive to enter into a careful examination of the detailed transactions of the corporation for the fiscal year, and, more often than not, they make a report based upon a conventional performance of their duties. A control exercised in this manner is worse than no control at all, because it gives the stockholders and creditors a false impression of security. It was for this reason, doubtless, that the Corporations Congress of 1900 expressed a desire that the control by auditors be entirely eliminated.³

In addition to these defects, there is much dissatisfaction with the attitude taken by the courts in actions against the directors for mismanagement. In the absence of palpable fraud, it is difficult to obtain redress in the courts. Thus, it has been said that the degree of severity which the courts exercise in repressing the evils of corporate management depends largely upon whether the losses have been sufficiently great to draw the attention of the general public.

¹ *Revue des sociétés*, 1894, p. 169.

² Nouel, *op. cit.*, p. 148.

³ Nouel, *op. cit.*, p. 150.

This applies even to transgressions coming within the definitions of the Penal Code.¹

2. GERMANY

Existing Law.—The many safeguards thrown round the interests of stockholders and creditors in the organization of corporations in Germany are reinforced by the control which the legislature has provided over the management.

The distinctive right of the shareholder is, of course, that of receiving a share of the profits of the corporation when earned. The shareholder has a more immediate control over the declaration of dividends than in England or America, as dividends are declared by the general meeting of stockholders and not by the supervising council or the directors.² German law is rigorous in its protection of the capital of a corporation from unwarranted disbursements to shareholders out of funds other than net profits. The Code expressly provides that interest cannot be paid upon shares except during a period preceding the beginning of operations; thereafter a distribution among shareholders can only be paid out of the net profits shown by the annual balance sheet.³ The sanction for this is found in making the shareholder himself responsible for the obligations of the company if he has accepted payments not permitted by the Code. Good faith, however, excludes such personal liability.⁴ Of course, in addition to the liability of the shareholder himself, the members of the supervising council

¹ Nouel, *op. cit.*, pp. 154, 155.

² German Comm. Code, sec. 260. The general meeting has also the exclusive right of accepting the annual balance sheet and discharging the directors and supervising council from liability for acts done in behalf of the corporation during the preceding period. *Ibid.* Cf. Staub, *op. cit.*, p. 787.

³ Comm. C., sec. 215.

⁴ *Ibid.*, sec. 217.

and directorate are also responsible if they have proposed the unlawful disbursements of dividends. The nature of their liability will be discussed hereafter.

A further guaranty that the capital of the corporation shall be employed only for the legitimate operations of the company is found in the provision prohibiting corporations from purchasing their own shares in the regular course of business, or accepting them in pledge.¹ The motive of the provision is stated to be two-fold: first, because it is repugnant to legal concepts that a corporation to be its own shareholder, and secondly, because the provision tends to prevent speculation in the shares of the corporation by its officers and managers, who might thus obtain unfair advantages on the credit of the organization.² It is to be noted that shares may not be purchased even out of the surplus. An exception is made where the purchase of shares is necessary to carry out plans of retirement or amortization. This, however, must have been stipulated in the articles of association. Unless a reduction of capital is contemplated, the purchase of shares for amortization must be made out of surplus profits only.³

Differing from the plan of corporate organization within the Anglo-American sphere, the management of the corporation is entrusted, not to a board of directors executing its mandates through officers, but to a managing directorate (*Vorstand*) consisting of one or more persons elected by the general meeting of stockholders (*Generalversammlung*), each being subject to recall at all times. The Code does not state whether the general meeting or the supervising council shall exercise the power of recall, but it is doubtless within the power of the council where the articles

¹ Comm. C., sec. 226.

² Staub, *op. cit.*, i, p. 679.

³ Comm. C., sec. 227.

of association have transferred to it the power of appointing the directors.¹ The important element is that the board of directors or managers constitutes the official representative of the corporation both in and out of court and is a necessary organ thereof.²

Acts of the directorate, like those of the trustees of an express trust under English law, require the coöperation or consent of all the members. This is carefully observed in practice, especially for transactions evidenced in writing. Of course, the articles of association (as the equivalent of the deed creating the trust) may provide otherwise; it is also permissible for the directorate to designate one of their number to have the power to engage singly in certain transactions or classes of transactions. Furthermore, the articles may provide that a permanent representative (*Prokurist*) of the corporation may act in conjunction with one of the members of the directorate.³

It is one of the objects of the commercial legislation of Germany, as indeed of that of many countries of the Continent of Europe, to protect corporations, partnerships and individuals against unauthorized acts, by compelling the designation of all authorized agents by written instrument registered at the commercial registry. This device is especially valuable for corporations, as it presents the opportunity for a system of checks and counterchecks upon the acts of officers. It also protects the public, in that the authorized agents of any corporation may be easily ascertained. The signatures of the members of the directorate

¹ Staub, *op. cit.*, p. 692. Ring, *Das Reichsgesetz betr. die Kommanditgesellschaften auf Aktien und die Aktiengesellschaften*, note 10 to article 2270; Behrend, *Lehrbuch des Handelsrechts*, sec. 124, note 20.

² Comm. C., sec. 231; Staub, *op. cit.*, p. 689.

³ *Ibid.*, sec. 232.

must be deposited at the court having charge of the registry.¹ Indeed, the Code makes the interest of the public paramount; for, while it permits the corporation to limit the operations of the directors, making them responsible to the corporation for any act *ultra vires*, third parties are not compelled to take notice of any limitation upon their powers. Thus, if the articles of incorporation limit their powers to certain classes of transactions, or permit them to act only under certain circumstances, or for a certain period of time, or at certain places, or subject to the consent of the general meeting, the supervising council or any other organ of the corporation, the limitation may be deemed ineffective as against third parties.²

The directors must devote all their time and skill to the business of the corporation. The corporation may either demand the benefits of any transaction outside the business or it may elect to claim damages.³ The directors may be compensated by a share of the annual profits, but all amortization and reserves must first be deducted.⁴ The directors are also charged with the keeping of proper books of account.⁵ If, in the preparation of any balance sheet, it appears that the corporation has lost half its capital, the directors must immediately call a general meeting of stockholders; whenever the corporation becomes insolvent, it is their duty to place it in bankruptcy.⁶

They must use the ordinary care of business men in the exercise of their office. Upon a breach of their duties they are liable for damages as joint debtors. The Code

¹ Comm. C., sec. 234.

² *Ibid.*, sec. 235.

³ *Ibid.*, sec. 236.

⁴ *Ibid.*, sec. 237.

⁵ *Ibid.*, sec. 239.

⁶ *Ibid.*, sec. 240.

specifically mentions certain examples of violations of the general duties already referred to.¹

The supervising council consists of three persons elected by the general meeting of the stockholders, unless the articles provide for a larger number.² It is not necessary that they be stockholders.³

It is customary on the Continent of Europe to compensate directors and supervisors by certain royalties (*tan-tièmes*) computed upon the net profits of the business. The German Code provides that no compensation shall be made to members of the supervising council until all amortization and reserves have been provided for and, in addition thereto, an amount set aside for distribution to stockholders equal to at least four per cent of the paid-in capital.⁴

It is stated to be the specific duty of the supervising council to keep watch over the management of the business of the company in all its branches and to be informed of the course of its affairs. It may demand a report from the directorate at any time; it has access to its books and writings, and may examine the condition of the cash account, securities and merchandise. It is its duty to verify and report upon the annual accounts and balance sheets, to make proposals for declarations of dividends and to advise the general meeting on all these subjects. It must convene the general meeting of stockholders when necessary for the interests of the corporation. Its further duties are determined by the articles of association. Its members may not delegate their functions to others, nor are they permitted to act one for another by proxy.⁵

¹ Comm. C., sec. 241.

² *Ibid.*, sec. 243.

³ Staub, *op. cit.*, p. 737.

⁴ Comm. C., sec. 245.

⁵ *Ibid.*, sec. 246. Staub explains that it is not objectionable for the board to assign certain duties to committees of their own number, but

As the directorate constitutes a separate organ of the corporation under the German law, the legislature has devised a system of checks and balances between that body and the supervising council. In most systems, the managers represent only a committee of the board of directors. Under German law, the members of the managing directorate have independent powers, but also separate responsibility. The supervising council represents the company in dealing with the directors and may bring suit against them when so authorized by the general meeting. If the responsibility of members of the supervising council is affected, it may bring suit against the directors, even though the general meeting may be opposed to the proceeding.¹

The separation of powers and responsibilities is carried out logically. The supervisors are prohibited from acting as directors, or as their permanent representatives; neither can they conduct the business of the company directly as its officers. A member of the supervising council may indeed become a director for a limited period in the place of an incapacitated director, but during this period he is not permitted to act as a member of the council. It is the clear intention of the legislature to secure at all times a complete separation of the two organs, in order that the one may control and be a check upon the acts of the other.²

The members of the supervising council are obliged to use the ordinary care of business men in the performance of their duties, and, in default thereof, they are responsible

the responsibility for final action is ascribable to the council as a whole. Votes upon resolutions cannot be made by proxy. *Op. cit.*, p. 748. This is contrary to the practice in some other European countries, *e. g.* Switzerland, where proxies at board meetings are permissible and customary. See Schneider and Fick, *Schweiz. Obligationenrecht*, pp. 498-501.

¹ Comm. C., sec. 247.

² *Ibid.*, sec. 248; Staub, *op. cit.*, p. 750.

to the corporation as joint debtors with the directors, for damages caused to the corporation.¹

A most salutary protection is provided against the exercise of voting rights in opposition to the liabilities which a shareholder may have incurred toward the corporation, while acting as a member of one of its organs. A shareholder may not vote upon a resolution which discharges or relieves him from the performance of a duty; nor can he vote as a proxy thereon. He is also prohibited from voting on a resolution relating to a transaction or litigation between the company and himself.²

The rule of publicity is applicable to all corporations. It is the duty of the directorate within three months from the close of each fiscal year to prepare a balance sheet and profit-and-loss account; also a report to the supervising council upon the financial condition and affairs of the company. These are presented to the general meeting with the comments of the council. The general meeting passes upon the report and acts upon the proposals for distribution of the profits. It discharges (*entlastet*) the directors and supervisors in the event of the complete performance of their duties.³

The Code provides in detail for the manner of preparing the annual balance sheet, imposing the duty upon the managers to take up the inventory at market values; where no market values are obtainable, the valuation must be no greater than cost. The amount of capital stock, as well as all reserves and renewal funds, must be taken up as liabilities; and, at the close of the balance, the profit or loss resulting from the difference between the assets and liabilities must be separately stated.⁴

In order to insure the *permanency* of dividends, the leg-

¹ Comm. C., sec. 249.

² *Ibid.*, sec. 252.

³ *Ibid.*, sec. 260.

⁴ *Ibid.*, sec. 261.

islature has made the creation of certain reserve funds obligatory. The reserves must include:

1. at least one-twentieth of the annual profits until the reserve amounts to at least one-tenth of the share capital;
2. a sum to cover the premium, if any, at which the shares were issued in excess of their par value;
3. a sum to cover assessments, if any, paid by shareholders in return for preferred rights, provided such assessments have not been made for the purpose of extraordinary amortizations or to replace extraordinary losses.¹

A minority of stockholders representing not less than one-tenth of the capital stock has power to adjourn the general meeting for the purpose of obtaining further information upon the specific items of the annual balance, and may continue to exercise this power until the report is fully explained.² It is true, the majority may determine that sufficient explanation has been given, but it does so at the risk of having the court nullify all subsequent resolutions of the meeting, if the demand of the minority is found to have been justifiable.³

A majority at the general meeting may appoint auditors for the purpose of testing the accuracy of the balance sheet, or of investigating transactions relating to the organization or management of the corporation. The legislature has here again protected minority interests in according to shareholders owning one-tenth of the capital stock the right to demand that auditors be appointed *by the court*, provided there be reasonable cause for believing that there has been unfairness, or gross violation of the law, or of the articles, in the preparation of the report.⁴ The managers must

¹ Comm. C., sec. 262. Subdivision 3 is for the purpose of assuring the application of the assessments to the objects for which they were levied. Staub, *op. cit.*, p. 808.

² Comm. C., sec. 264.

³ Staub, *op. cit.*, i, p. 814.

⁴ Comm. C., sec. 266.

submit the books and writings of the company to the auditors and permit them to examine into the condition of the company and of its securities and merchandise. The auditors must, without delay, file the results of their examination at the commercial registry.¹

As soon as the balance sheet and profit-and-loss account have been approved by the general meeting, they must be published in the official publications designated in the articles, and the entire report, with the comments of the supervising council, must be deposited at the commercial registry.

The penal provisions sanctioning the regulations of the Code relating to the *management* of the corporation are also specifically set out in the Commercial Code itself. Thus, members of the supervising council or directorate (or liquidators) who have wilfully acted contrary to the interests of the corporation are punishable by imprisonment not exceeding five years and by fine not exceeding twenty thousand marks, in addition to the loss of civil rights. In the event of extenuating circumstances, a fine alone may be imposed.² In this connection it is interesting to note that the courts are not inclined to impair the salutary effect of the criminal provisions of the statute by mild or lenient interpretation. Contrary to the practice of the courts in France, the penal provisions have been rigorously applied. Thus, directors have been punished even for injury to the corporation resulting from their wilful *omission* of duty.³

Misrepresentations made by members of the board of directors, supervising council (or liquidators) in their official capacity in respect of the financial condition of the corporation, more especially when made at the general meeting of stockholders, subject the offender to imprisonment

¹ Comm. C., sec. 267.

² *Ibid.*, sec. 312.

³ Decisions of the Imperial Court, Crim. Div., xi, p. 414.

not exceeding one year and to a fine not exceeding twenty thousand marks. Extenuating circumstances may permit the court to limit the punishment to a fine.¹ A penalty of imprisonment not exceeding three months and fine not exceeding five thousand marks is imposed upon members of the supervising council and board of directors (or liquidators) if the corporation has been permitted to continue without a council for a period of three months, or if the number of supervisors has been permitted to fall below the legal requirements. The same penalty is imposed upon directors (or liquidators) for failing to place the corporation in bankruptcy when it has become insolvent.

These penalties apply, however, only to individual wrongdoing. It may well be that a member may have undertaken to act and been opposed by the other members;² or may have obtained advice of counsel as to his duty in the premises and may have been informed that no action was necessary. In such cases defendants have been held blameless.³

The proper exercise of voting rights is safeguarded by a provision imposing imprisonment not exceeding one year and fine not exceeding ten thousand marks upon any person who knowingly falsifies or forges a certificate of deposit of shares or interim certificates for the purpose of voting thereon at a general meeting.⁴ Furthermore, any shareholder who has agreed, in consideration of special advantages, to cast his vote in a certain manner at a general meeting, or to abstain from voting, is punishable by a fine not exceeding three thousand marks, or imprisonment not exceeding one year; the same penalty is imposed upon

¹ Comm. C., sec. 341.

² Staub, *op. cit.*, i, 942.

³ Decisions of the Imperial Court, Crim. Div., v, 161.

⁴ Comm. C., sec. 310.

the person offering the bribe.¹ The section applies not only to shareholders, but also to their proxies.

Any person who assumes to vote upon the shares of another without authorization, or who borrows the shares for a consideration for that purpose, is punishable by fine of from ten to thirty marks upon each share voted upon or borrowed, and the fine shall be not less than one thousand marks.²

The law regulating stock exchanges imposes a penalty of imprisonment and fine not exceeding fifteen thousand marks upon any person who knowingly and with fraudulent intent makes a false statement in a prospectus or public advertisement, for the purpose of obtaining subscriptions to corporate securities, or for the purpose of effecting a purchase or sale thereof.³

Comment.—The social tendencies of modern legislation are observable even in the domain of purely private law. Nowhere is this more marked than in the body of laws promulgated in Germany at the end of the nineteenth century. The corporate form of business is manifestly regarded by the legislator as a facile means of exploiting the less favored classes and, accordingly, a strict control is exercised over all administrators of industrial corporate wealth. It is therefore the *internal régime* of the corporation which is made the object of regulation, rather than the functioning of the corporation as a legal entity. Legislative consciousness has not reached this development in the United States, where regulation continues to be *qua* the corporation rather than *qua* its administrators. The need for a change of legislative attitude is evidenced by the increasing number of small shareholders of moderate means holding corporate securities.

¹ Comm. C., sec. 317; *cf.* note to Staub, *op. cit.*, p. 943.

² Comm. C., sec. 318.

³ *Börsengesetz*, sec. 75.

Ihering pointed out that the status of an administrator of group property is the most dangerous to society of any known to the law. Immediate contact with the property of others gives him both the desire and the opportunity of appropriating it to his own use. No thief can steal so easily as an administrator; nor can any swindler so readily arrange and accomplish a fraud. Ihering concludes by demanding the greatest number of guaranties where the danger is most imminent.¹

The tripartite organization of the German corporation is especially designed to prevent the breach of the fiduciary relationship of its administrators. The three organs are respectively those of general administration, operative management and financial control. While each acts as a check upon the other, the court exercises a supervision over all. Nor is its control merely negative. German courts do not hesitate to issue affirmative mandates in the interest of sound business.²

The German Code is complete in respect of the sanctions which it establishes to secure the performance of the duties of the corporate functionaries. In all aggravated cases, criminal penalties are provided. In any event, creditors and shareholders have a direct interest in being watchful and diligent, because their rights of action are individual as to themselves and direct as to the functionary. This theory of direct remedy continues until the period of bankruptcy, when it is assumed that the official liquidator will protect the interest of all.³

¹ *Der Zweck im Recht*, i, 226.

² See e. g. 64 Decisions of the Imperial Court, Civil Cases (1907), p. 258, interpreting sec. 271 of the Commercial Code so as to effectuate the right of shareholders to compel the administrators to make the proper reserves and amortizations. The court's action did not limit itself to nullifying an irregular act but directed the proper one.

³ 74 Decisions of Imperial Court, Civil Cases (1911), p. 428.

German legislation thus surrounds the operation of corporations with the most effective guaranties for the protection of investor and creditor. Its critics, especially in foreign countries, accentuate its complexities and severities, but few question its adequacy.¹

3. ITALY

Existing Law.—The management of corporations in Italy is entrusted to a board of directors who may, if they so choose, delegate executive functions to one or more of their own number acting as a managerial committee.² The Commercial Code provides also for a separate organ of supervision, as in Germany.³ It provides, therefore, a much more effective control over the acts of the directors than the French Code.

The directors serve for a period designated by the articles, not exceeding four years. If the articles fail to mention a period, the directors serve for two years.⁴ If all the directors are elected at the same time, the term of one-half of their number must not exceed one-half the period designated by the articles. The directors must qualify by depositing shares of the company as security, amounting in the aggregate to at least two per cent of the capital stock.⁵

Italian law is explicit in defining the direct responsibility of directors to shareholders and creditors ("*terzi*," lit. third parties). Directors are subjected to a joint liability

¹ Marinesco, *op. cit.*, p. 341.

² By the Italian law, the power of engaging and discharging employees (*impiegati*) is specifically entrusted to the board of directors unless the corporate statutes reserve it to the general meeting of shareholders. Comm. C., art. 143.

³ Syndics; *cf. infra*, pp. 137 *et seq.*

⁴ Comm. C., art. 124.

⁵ *Ibid.*, art. 123. The articles may provide for the deposit of a definite sum not to exceed 50,000 lire.

for a violation of their duties in connection with the following subjects: ¹

1. in respect of the actual payment of the share capital;
2. in respect of the payment of dividends from earnings only;
3. in respect of the keeping of books of account as prescribed by law;
4. in respect of the faithful execution of the resolutions of the general meeting;
5. in respect, generally, of the exact observance of the duties imposed upon them by law, by the articles and by the corporate statutes, unless such duties result from a limited and individual mandate.

Wherever the duty of the director is individual, the joint liability of the other members ceases, notwithstanding the fact that the individual duty is subject to the control of the board.² So, too, even where the duty is joint, an individual director may avoid responsibility by refusing to unite with his co-directors and disavowing their acts.³

Directors are prohibited from acting as proxies for stockholders; ⁴ from voting upon resolutions in which they have a personal interest; ⁵ and from voting upon resolutions relating to acceptance of the annual balance sheet or affecting their responsibility as directors.⁶ They, as well as the syndics ⁷ and other representatives of the corporation are relieved of their functions, as a matter of law, when they

¹ Comm. C., art. 147.

² *Ibid.*, art. 148; similar in this respect to the French L. of 1867, art. 44.

³ *Ibid.*, art. 149; similar in this respect to the German law. Cf. Staub, *Kommentar*, i, p. 730, n. 7.

⁴ Comm. C., art. 160.

⁵ *Ibid.*, art. 150.

⁶ *Ibid.*, art. 161.

⁷ The functions of these officers are described *infra*.

lose capacity to act, or have been sentenced for a criminal offense, or for a correctional offense involving fraud, embezzlement, or swindling (*truffa*).¹

The general meeting determines whether action shall be brought by the corporation against the directors. The action itself is then prosecuted by the syndics. The individual stockholder, however, may complain to the syndics of an act of the directors deemed by him to be irregular. The syndics must make mention of the complaint in their annual report, and if the complaint is made by shareholders holding at least one-tenth of the capital stock, the syndics must report conclusions and proposals in respect of the same. If the syndics deem the complaint well founded and action urgent, a general meeting must be immediately convened.²

Besides the protection afforded to the stockholders by complaint to the syndics, a direct appeal to the commercial court may be made by stockholders holding one-eighth of the capital stock against grave irregularities in the performance of the duties of the directors. The court may order an examination of the books by experts, and if the complaint be substantiated, the court may take such emergency steps as may be called for, and immediately convene a general meeting of stockholders.³

Italian law is noteworthy in the protection which it ac-

¹ Comm. C., art. 151.

² *Ibid.*, art. 152. A vote of the general meeting in violation of some provision of the corporate statutes, even though by an overwhelming majority, may be nullified at the suit of a single stockholder before the courts. Court of Appeal, Turin, Sept. 5, 1887; *Annali di giurisprudenza*, xxi, pt. ii, p. 423.

³ *Ibid.*, art. 153. The credit of the corporation is conserved by a provision that if the complaint be not sustained, that fact shall be published in the official journal. The complainants must furnish security for the costs of the proceeding. *Ibid.*

cords to minority interests. A three-quarters quorum, with an affirmative vote of a majority of all the outstanding stock, is required in the following instances:

1. Dissolution prior to expiration of the term.
2. Extension of duration.
3. Merger.
4. Decrease of capital stock.
5. Reclassification or increase of capital stock.
6. Change in the objects of the corporation.
7. Any other amendment of the articles.¹

Minority stockholders opposing a resolution which extends the duration of the corporation, or authorizes a fusion, or reclassifies or increases the capital stock, or changes the objects of the enterprise are entitled to retire (*recedere*) by redeeming their shares on the basis of their value as shown by the balance sheet last accepted.²

The share certificates of Italian corporations, whether bearer or registered, are required to state (besides the usual data, namely, title and capitalization) the date of the articles and of the publication thereof, the place where published and the duration of the corporation.³ The shares must remain registered until fully paid up.⁴

A salutary check upon the overissue of funded securities is found in the provision that no corporation may issue bonds for an amount exceeding the unimpaired paid-up capital stock unless the excess is guaranteed by a deposit of national, provincial, or communal bonds.

The so-called "syndics" (*sindaci*) provided for by the Code⁵ occupy a position of much greater importance than

¹ Comm. C., art. 158.

² *Ibid.*

³ *Ibid.*, art. 165.

⁴ *Ibid.*, art. 166.

⁵ *Ibid.*, art. 183. Their number is three or five, [with two substitutes] appointed at the constitutive meeting and at each regular meeting

the auditors or revisors of the other Continental systems. Their duties are as follows: ¹

1. To determine the form of the balance sheet and the condition of the capital stock;
2. to examine the books of account at least once a week and to be informed of the operations of the company and the validity of its written documents;
3. to verify the cash at unexpected moments (*improvisto*) at least quarterly;
4. to control the possession of securities held as pledge, guaranty, or in the treasury;
5. to insure compliance with the conditions mentioned in the articles and corporate statutes for participation of stockholders in the general meetings;
6. to examine and test the correctness of the balance sheet and make report thereon to the general meeting;
7. to superintend liquidation;
8. to convene the general meeting where the directors fail to do so;
9. to participate in all general meetings;
10. generally to observe that the directors comply exactly with the provisions of law, of the articles and of the corporate statutes.

They have the right to demand that report be given them monthly of the operations of the company; they may be present at all directors' meetings and may suggest the subjects which shall constitute the order of business.

It is to the syndics that the annual report of the directors is presented, one month before the annual meeting.² The syndics base their proposals upon the report, which, together

thereafter. They need not be stockholders but must not be related by blood or marriage within the fourth degree to any of the directors. Their functions are very similar to those of the German *Aufsichtsrath*.

¹ Comm. C., art. 184.

² *Ibid.*, art. 176.

with the balance sheet and the minutes of the meeting, must be filed within ten days after the meeting with the clerk of the commercial court. Publication of the balance sheet is compulsory.¹

In Italy, as in other Continental European countries, a reserve fund must be created. Five per cent must be credited to the reserve annually before dividends can be declared, until the fund amounts to one-fifth of the capital stock.²

Like the German Code, the Italian Commercial Code includes among its provisions the *criminal* penalties applicable to violations of the mandatory rules of corporate management.³

4. SPAIN

Existing Law.—The management of the operations of corporations is entrusted by Spanish law to the directors (*administradores*), whose tenure and manner of election by the shareholders (exclusive of the members of the board) is determined by the articles and the corporate statutes and regulations.⁴ The phraseology employed by the Code indicates that the practice prevailing elsewhere of

¹ Comm. C., arts. 180, 94, 95.

² *Ibid.*, art. 182. Of course no dividends can be declared except out of earnings. *Ibid.*, art. 181.

³ Any organizer, director, syndic or liquidator who makes a wilfully false statement to the general meeting in respect of the condition of the company's affairs, or who is responsible for distribution of unearned dividends, or for issuing stock below par, or for purchasing shares of the company except as permitted by law, or for issuing obligations exceeding in the aggregate the capital stock, or for reducing the capital stock or consolidating otherwise than permitted by law, is punishable by a fine not exceeding 5,000 lire, in addition to such other and more severe penalties as the Penal Code may prescribe under its general definitions. Art. 247.

⁴ *Código de comercio*, art. 155.

appointing a managerial committee prevails also in Spain, but there is nothing to show that the managers (*los gerentes*)¹ have any powers or duties other than those conferred on them by delegation from the board.

Corporations must publish monthly in the *Gaceta*, or official newspaper, a detailed balance sheet of operations, with an inventory stating the value of all property and effects capable of being estimated.²

Shareholders may verify the accounts and have access to the vouchers proving the same.³ This right is greatly limited, however, by the provision of the Code restricting its exercise to such times as may be prescribed by the corporate statutes and regulations.⁴

In order that the general meeting may validly vote an increase or decrease in the capital stock, at least two-thirds of the entire number of stockholders must be present, representing two-thirds of the par value of the outstanding stock. If the capital of the company remaining unimpaired exceeds seventy-five per cent of the debts and obligations of the company, at the time a resolution is passed in favor of such increase or decrease, it may be immediately effectuated, provided all creditors holding claims at the time assent or are paid.⁵

5. SWITZERLAND

Existing Law.—Swiss law provides three independent organs through which the operation of corporations are conducted. Instead, however, of a board of management controlled by an independent council of supervision, as in Germany and Italy, it provides a board of directors whose

¹ Comm. C., art. 173.

² *Ibid.*, art. 157.

⁴ *Ibid.*, art. 158.

³ *Ibid.*, art. 173.

⁵ *Ibid.*, art. 168.

duty it is to manage the company either directly, or through a committee of their own number, subject only to an annual audit by a board of control (*Controlstelle*) or auditors who report to the general meeting upon the acts of the board of directors. Accordingly the organs recognized by law are the general meeting, a managing board or board of directors and a board of auditors.¹

The general meeting must be called either by the board of directors or, if necessary, by the auditors, within six months after the close of the fiscal year. It has exclusive power to pass upon the balance sheet submitted by the directors, and to declare dividends; its resolutions must, however, be preceded by a report of the auditors.²

Shareholders holding one-tenth of the capital stock may, by request in writing, compel the convening of special meetings of stockholders.³

It is quite customary in Switzerland to elect the directors for a longer period than one year; they may indeed be elected for a period not exceeding six years and are then re-eligible thereafter.⁴

The representation of the corporation is exclusively in their hands. They may, however, delegate their authority to a managing committee (*Direktion*) or to individual representatives (*Prokuristen*). Such a delegation of authority must be evidenced by documents registered at the commercial registry, in the absence of which all the directors must assent or subscribe to acts done in the name of the corporation.⁵

Switzerland contains a large number of industrial es-

¹ Code of Oblig., arts. 642-663.

² *Ibid.*, art. 644.

³ *Ibid.*, art. 645.

⁴ *Ibid.*, art. 649.

⁵ *Ibid.*, arts. 651, 653; Schneider and Fick, *op. cit.*, p. 500.

tablishments of great importance; indeed, the operations of its financial institutions extend throughout the world. Owing to its limited natural resources, the energies of its people have been directed to mercantile enterprises both within and without the national territory, most of which, however, are controlled by domestic corporations. It is not surprising, therefore, that its corporation laws should contain detailed provisions gained from practical experience, tending to secure a conservative system of management and accounting beneficial to stockholder and creditor alike.

Its compulsory system relating to annual accounts is worthy of special mention. The annual balance sheet must be prepared so as to give the shareholder "a true insight into the actual financial condition of the corporation":¹

(1) Costs of organization and administration must be charged as expenses.² Such organization expenses as have been provided for in the corporate statutes or resolutions of the general meeting may be divided into equal parts and written off over a period not exceeding five years.

(2) Lands, buildings and machinery must not be valued above cost, less the proper amortization according to circumstances. The amount of insurance carried must be stated.

(3) Securities having a market value must not be valued above the average market price for the month prior to the date at which the balance is taken.

(4) Merchandise must not be valued above the cost price, nor, if this be higher than the market value, above the market price.

(5) The aggregate of doubtful accounts and the aggregate of amortizations must be stated.

¹ Code of Oblig., art. 656.

² This provision contrasts favorably with the practice so often met with in the United States of carrying the organization expenses as an asset, at least over a considerable period of years.

(6) The amount of the capital stock as well as reserves and renewal funds must be taken up as liabilities.

(7) Bonds issued by the company must be stated at the full amount necessary for their payment. However, the difference between the issue price and the amount to be repaid, which must be liquidated by annual amortizations to the date of maturity, may be taken up as assets.¹

The provisions governing the civil responsibility of directors and auditors are so similar to those of the German Commercial Code as not to require detailed consideration. It is interesting to note, however, that the criminal sanctions could not be made part of the Code of Obligations because, penal law not being within the scope of *federal* legislation, they would have been unconstitutional.² Accordingly, criminal penalties, if any, must be sought for in the laws of the separate cantons.

¹ Code of Oblig., art. 656.

² Schneider and Fick, *op. cit.*, p. 519, n. 2.

CHAPTER VII

LEGISLATION AND REFORM IN ENGLAND AND AMERICA.— OPERATION

Publicity.—The English law, unlike that of Continental European countries, contains no special provisions with respect to the preparation of an annual balance sheet. There is, however, a “statutory report” which must be forwarded to all shareholders seven days before the *first* general meeting. This must contain a detailed statement of the receipts and disbursements on account of capital.¹ The first meeting must be held not less than one nor more than three months from the time at which the company is entitled to begin business. Although a general meeting of every company must be held at least once every calendar year,² the act does not provide for a compulsory financial report. Peculiarly enough, however, the appointment of an auditor or auditors at each annual meeting is compulsory. As on the Continent of Europe, the auditors constitute a true board of control, directors and officers being ineligible.³ Every auditor has the right of access to the books, accounts and vouchers of the company and is entitled to such information as the directors and officers may be able to give in connection with the audit. It seems to be assumed that a balance sheet will be laid before every company at general meetings, for it is provided that the auditors shall make a report to the shareholders, not only on accounts examined by them, but also on the balance sheet, stating:

¹ Companies Act, 1908, sec. 65. ² *Ibid.*, sec. 64. ³ *Ibid.*, sec. 112.

(a) Whether or not the auditors have obtained all the required information;

(b) Whether in their opinion the balance sheet exhibits a true and correct view of the condition of the company's affairs as shown by the books.

The act therefore accomplishes indirectly what the German statute makes compulsory.¹ It is provided under penalty of a heavy fine that whenever a balance sheet is issued, circulated or published, it must be accompanied by a copy of the auditors' report. This is analogous to the indirect control which the act provides over the issue of shares for property by its regulations in respect of the prospectus.

The legislation of the American states is far less protective of the interests of creditors and stockholders than either that of England or that of other European states in the matter of making and publishing reports. Most of the legislation referring to the publicity of the affairs of industrial corporations relates to reports made obligatory for the purposes of taxation. These vary greatly, according to whether legislation demands detailed statements of assets and liabilities, or a general statement of assets and liabilities, or a general statement of the amount of capital paid in and the proportion invested within or without the state.² These reports are disclosed neither to the general public nor to parties interested. Under ordinary conditions, access can be had only by mandamus proceedings.³ But even were they entirely open to inspection, reports made for the purpose of taxation are apt to be manipulated, if not directly falsified, and would be of little service to creditor or stockholder in judging the operations of the

¹ See Buckley, *Company and Limited Partnership Acts*, (1900), p. 267.

² Horack, *op. cit.*, p. 88.

³ *Ibid.*, p. 87.

company and the conservation of its assets. During the past two decades, a strong popular movement has been tending toward publicity in favor of persons entitled to the information in addition to reports made to the state. The Report of the Industrial Commission appointed by Congress in 1898 recommends:

The affairs of a corporation or industrial company should be carried on without detriment to the public, in the interest of its members and under their lawful control, and to this end the directors or trustees should be required:

(a) To report to the members thereof its financial condition in reasonable detail, verified by a competent auditor, at least once a year;

(b) To inform members regarding the methods and conduct of business by granting, under proper restriction, access to records of directors' meetings, or otherwise;

(c) To provide for the use of members, before the annual meeting, lists of members with their address and their several holdings; and

(d) To provide, in whatever other way may be named in the certificate of incorporation, means whereby the members may prevent the misuse of their property by directors or trustees.¹

An approach toward compulsory publicity in favor of the stockholder is already discernible in some states. A general provision is sometimes found requiring a true statement of the accounts of the corporation to be rendered annually to the stockholders.² But these provisions are

¹ Report of Industrial Commission, vol. xix, p. 649, being House Doc. no. 380, 57th Congress, 1st Session.

² Wis. Sanborn's Stats., sec. 1750; Mich. Corp. Act 1903, sec. 15; Mo. R. S. 1909, sec. 3349. The law of Ohio requires that a full statement of the condition of the company's affairs together with a list of stockholders be mailed to each stockholder at least ten days before the election. Gen. Code, 1910, sec. 8685.

either directory only, or else a penalty of moderate amount is provided to be recovered at the suit of a stockholder for non-compliance.

The Draft Act of the Commissioners of Uniform State Laws provides that annual reports be filed in the office of the secretary of state, giving the amount of assets and debts; a fine shall be imposed if the report is not made and filed within ten days after written request by any creditor or stockholder.¹ The draft fails to distinguish between reports made for state and those for private purposes; it confounds the usual tax report with such a financial statement as interested parties should be entitled to.

The publicity provided for by the proposed bill for federal incorporation is of a wider character than any general provision found in the state statutes. An annual report is to be filed with the commissioner of corporations, setting forth such details as the commissioner himself "shall from time to time prescribe," the report to be signed by at least three directors. The commissioner is given the power to call for special reports whenever in his judgment the same are necessary for a full and complete knowledge of the condition of a corporation.² Nowhere does it appear, however, that such information, when given, or on file, is intended for the benefit of and accessible to creditors or stockholders. This should not be left open to conjecture.

As a whole, publicity should be compulsory at or shortly before the annual meeting. Moreover, legislation should adjust itself to the actual processes of business. For ex-

¹ Second Tentative Draft, p. 26, sec. 25. The provision is similar to that of the New York statute, except that the latter permits the debts to be stated by maximum and the assets by minimum figures and suit to recover the penalty prescribed must be brought by the people of the state. *Stock Corp. L.*, rev. 1910, sec. 34.

² Senate Bill no. 6186, 61st Cong. 2nd Session, sec. 18.

ample, we have seen that Switzerland and Germany, by regulating the form and scope of the balance sheet in accordance with the principles of skilled accountancy, have caused the statement to conform to an uniform system comprehensible to all.¹ The rules of the principal stock exchanges in the United States have helped to bring information to interested parties which they would never have received under the present condition of the law; but as there are only a comparatively small number of corporations whose securities are listed, general relief must be sought in legislation.

Protection of Minority Shareholders.—Professor Burgess has said: “When the government confers upon a number of persons, forming a corporate body, the power to do business by the will of a quorum and majority of them, sound political science requires the government to insure that the majority shall not so abuse this power as to deprive the individuals who happen to constitute the minority of any of their civil or political rights, as guaranteed to them by the constitution and laws of the country.”²

The rule of the majority is usually considered essential to the existence of democratic institutions.³ But this should not mean that the minority is to be placed at the absolute mercy of the majority. In order to prevent this in the management of corporations, means analogous to those employed in political elections have been adopted for giving the minority proportional representation in the board of directors.

¹ See *supra*, chap. vi, subdivs. 2 and 5.

² *Op. cit.* *Political Science Quarterly*, 1908, xiii, p. 205.

³ Savigny intimates that the right of the majority to determine the will of the corporation is a result of natural law. *System des heutigen römischen Rechts*, bk. ii, ch. ii, sec. 97.

The English statute does not provide for proportional representation, although nothing would seem to prevent the regulations from granting to the stockholders the right of cumulative voting. This may well be accomplished also by the by-laws under the laws of the states; but some states have gone further and have provided for a compulsory proportional representation. Thus, in Illinois, Kansas, Missouri, Michigan, Nebraska, Ohio, South Carolina and some other states, in all elections of directors or managers of corporations, every stockholder shall have the right to vote in person or by proxy for the number of shares owned by him for as many persons as there are directors or managers to be elected, or to cumulate his vote by giving one candidate as many votes as the number of directors or managers multiplied by the number of his shares of stock shall equal, or to distribute his vote on the same principle among as many candidates as he shall think fit.¹

This device has not been accepted by the Commissioners of Uniform State Laws. Neither is it to be found in the bill for federal incorporation. Its use in practise, however, would constitute a salutary check upon the arbitrary or selfish acts of directors, since it at least permits the minority to be apprised of matters concerning which they would otherwise be left in total ignorance.

Holding Companies.—Undesirable as it is for the majority to manage the company to the detriment of the interests of the minority, it is equally undesirable that corporations, through the device of a holding company, should

¹ Ill. Gen. Corp. L., sec. 3; Kans. Gen. Stats., 1909, sec. 1746; Mo. Const. art. xii, sec. 6; Mich. Pub. Acts as amended 1907, no. 141 and 1911 no. 268; Neb. Const. art. xiii, sec. 5; Ohio, Gen. Code, sec. 8636; S. C. Civ. Code, 1902, sec. 1846. Optional in Minn. R. L. 1905, sec. 2862; N. Dak. Const. art. vii, sec. 135; N. J. Corp. Act rev. to 1910, sec. 35a; N. Y. Gen. Corp. L. rev. to 1910, sec. 24; Utah, Comp. L. 1907, sec. 335; and other states.

be placed in the control of persons holding a minority of its capital stock. The power of corporations to hold the shares of other corporations for all purposes is of practically recent origin. It was denied them by the common law unless necessary to subserve the purposes for which the corporation was organized. However, legislation during the last half century generally favored it, as tending to promote and enlarge the usefulness of the corporate form. It has been said that in America it has resulted from the competition between the states in bidding against one another for the patronage of corporations.¹ The power is recognized by the English Act and exists also on the European Continent.²

Where one corporation holds stock in another the shares may be and frequently are voted upon in the interest, not of the subsidiary, but of the parent corporation. Therefore, when the parent corporation holds a majority of the stock, injustice to the minority interests of the subsidiary is frequently the result.

The device of the holding company also provides a method by which even a minority may be in control of the subsidiary. If A. owns 26 per cent and B. 25 per cent of the stock of a corporation, making together 51 per cent, and if they transfer their holding to a company formed for the purpose of holding the stock of A. and B., then A. as the owner of the majority of stock in the new company,

¹ Untermyer, *Some Needed Legislative Reforms in Corporate Management*, (1911), p. 3.

² Companies Act, 1908, sec. 68. Germany, see Staub, *op. cit.*, sec. 182, n. 4; sec. 210, n. 4, according to which a corporation may even be one of the organizers of another corporation. In Switzerland, Italy, *etc.*, the power is not expressly granted but follows as one of the incidents of legal entity. The corporate statutes may acknowledge it or limit it. Lehmann, *op. cit.*, i, p. 255 and note.

which he receives in exchange for the 26 per cent of the subsidiary, is left in control of the subsidiary. The scheme has actually been adopted in practice, both in respect of railroads and industrial companies, thus circumventing the prohibition contained in the statutes against voting trusts.¹

The Federal Incorporation Bill prohibits any corporation organized under the act to acquire or hold stock in any other corporation; and no corporation organized under a state law or that of a foreign country may hold stock in a corporation organized under the federal act if engaged in carrying on a like business.² Although the primary purpose of this enactment would seem to be to prevent monopolies and combinations, it would also tend to conserve the interests of stockholders generally, by returning to the era of a group type composed of individuals, operated according to the checks and balances of human interest. If indeed a corporation has no soul, the device of the holding company presents a soulless group-type of members themselves soulless.

The President of the United States seems to have regarded the prohibition against holding companies contained in the Federal Incorporation Bill as one of its most salutary features.³

Direct Responsibility of Officers and Directors.—We have seen that under Continental European law a direct liability is created in behalf of an injured creditor or stockholder against a director or manager guilty of the breach of a specific duty. This is not the rule of English and Amer-

¹ See Untermyer, *op. cit.*, p. 12; N. Y. Gen. Corp. L. sec. 25 limits these agreements to five years and extends the privilege of participation to all stockholders equally.

² Senate Bill, no. 6186, 61st Cong. 2nd Sess., sec. 8.

³ See Special Message of President Taft, January 7th, 1910.

ican law. The liability of a director is primarily to the corporation, and he is responsible only to it for a breach of trust. Action must therefore be brought in the name of the corporation or of all stockholders equally interested.¹ In such a proceeding the plaintiff has a diminishing interest in proportion to his obligation to share the advantages of his diligence with others. Of course, a manager or director should not be harassed with litigation brought on account of fancied injuries. The creditor must prove his claim against the corporation. If judgment is returned unsatisfied, a specific breach of duty resulting in a loss to the corporation might very well constitute a direct cause of action, if the breach was the proximate cause of the creditor's inability to collect his claim. The shareholder should have a direct remedy also where the value of his shares has been impaired by a specific breach of duty, not a mere error of judgment, on the part of the director or manager.

This ideal has not been definitely evolved in our jurisprudence, although suggestions for reform point toward establishing direct remedies in certain cases. The draft of the Commissioners of Uniform State Laws provides that if the bonded indebtedness of a corporation exceeds the amount of its paid up stock, or if any dividends are declared other than from net profits, or if a reduction of capital be made under the guise of a loan to stockholders, or if any report or statement required by law is false in any material representation, all assenting directors shall be jointly and severally liable to the creditors of the corporation for any loss or damage arising therefrom.²

Criminal Penalties.—We have asserted that the trust

¹ *Menier v. Hooper's Teleg. Works*, 1874, L. R. 9 Ch. App. 350; *Mason v. Harris*, 1879, L. R. 11 Ch. D. 97; *Hawes v. Oakland* (1881), 104 U. S. 450.

² Second Tentative Draft, sec. 22.

relation may be made most effective by recognizing a direct responsibility to the real parties in interest. Where the breach of the relation is willful, the fiduciaries should be subjected also to criminal penalties; and the wrongful acts should be defined and the penalties stated in the statute enacting the duty, not left to the broad and vague provisions of general codes of criminal law. The criminal sanctions form an integral part of the law of corporations in Germany and Italy.¹ Many of the states have made a beginning in this direction in respect of penalties for declaration of unearned dividends or for making false reports. Recently a number of the states have gone far beyond this, and have enacted what might be termed a petty code of criminal law applicable to the officers of corporations. Thus, California makes the penal rules regarding embezzlement applicable to any officer, director or agent of a corporation who fraudulently appropriates to any use or purpose not in the due and lawful execution of his trust any property which he has under his control.² Any officer or agent of a corporation who knowingly exhibits any false, forged or altered book or paper to any public officer authorized to examine its affairs is punishable by imprisonment in the state prison for not less than three nor more than ten years.³ The Code defines as a misdemeanor the act of any person who inserts the name of another in any prospectus, circular or other advertisement of a corporation, in order to lead persons into the erroneous belief that the person whose name is so inscribed is an officer, agent or promoter of such corporation.⁴ Every

¹ See *supra*, subdivs. 2 and 3.

² Penal Code, sec. 504.

³ *Ibid.*, sec. 558.

⁴ *Ibid.*, sec. 559; *semble*, Wash. 1903, p. 141; Ore., Lord's Laws, sec. 2024, 2025.

director, officer or agent who receives any money or property of the corporation otherwise than in payment of a just demand, and who, with intent to defraud, omits to make true entry thereof in the books, or who falsifies any of the books or papers of a corporation, is punishable by imprisonment in the state prison for not less than three and not more than ten years.¹

An examination of the various criminal provisions found in the legislation of the American states shows a striking lack of uniformity and an absence of any definite rule upon which to predicate criminal responsibility. In some states, the legislation is minute and specific, in others merely fragmentary.²

¹ Cal., Penal Code, sec. 563.

² See *e. g.*, Me. R. S. ch. 47; Md. Rev. Corp. Act, 1908; N. J. Pub. L., 1906, p. 549; N. Y. Pen. L. secs. 890, 661, 662, 665, 667. In Washington, fraudulent "puffing" in a prospectus or advertisement is made punishable with imprisonment of not less than one nor more than five years, or by fine not exceeding \$2000, or both. L. 1903, sec. 1, par. 141.

CHAPTER VIII

PROTECTION TO CREDITORS AND SHAREHOLDERS IN CONTINENTAL EUROPE—DISSOLUTION

I. FRANCE

Existing Law.—The dissolution of corporations is not regulated in the Commercial Code, nor in any succeeding statute. Certain provisions applicable to associations generally are considered applicable also to corporations. Of course, the expiration of the period of duration of the corporation, as mentioned in the articles of association, effects a dissolution of the corporation. The general meeting, by its power to alter the corporate statutes, has thus the indirect power of accomplishing a dissolution.¹

Other methods by which dissolution may be effected are provided in the Law of 1867.² In the event of an impairment of the capital stock to the extent of three-quarters, the directors are compelled to call a general meeting of all of the shareholders, and the shareholders may then decide whether the corporation shall be dissolved. The general meeting has power to continue the corporation notwithstanding the impairment of its capital. If the directors fail to convene the meeting as provided by law, any interested party may demand the dissolution of the corporation before the courts.

¹ Civil C., art. 1865; Lyon-Caen and Renault, *Manuel de droit commercial*, p. 245.

² Art. 37.

. 417]

Any party may demand a dissolution of the corporation if the number of the shareholders has been reduced to less than seven and remains so reduced for a period of at least one year.¹

French law is equally fragmentary in its provisions relating to the publication of the dissolution. The only express provision is to be found in article 61 of the Law of 1867, which requires that all documents and deliberations having for their object the dissolution of a corporation shall be published. Accordingly, publication is essential only in the event that it occurs through the voluntary act of the shareholders, as by a change in the corporate statutes respecting the duration of the corporation. On the other hand, no publicity would seem to be required where the corporation is dissolved by expiration of the time originally fixed; it is even doubtful whether a decree of dissolution pronounced by a court requires publication.²

French law also lacks any express provision relating to the *process* of liquidating a corporation. It would seem to be determined by the general principles of law and by such rules as are deducible from the "very intent" of the liquidation.³

In general, it may be stated that the court will be governed by the will of the shareholders in the appointment of liquidators, provided there be substantial agreement, in the absence of which the court will appoint its own liquidators. In Paris, there exists a syndicate of professional liquidators under the supervision of the tribunal of commerce, from whose number the liquidators of corporations are customarily chosen.⁴

¹ L. 1867, art. 37.

² Lyon-Caen and Renault, *op. cit.*, pp. 250-251.

³ *Ibid.*, p. 251.

⁴ *Ibid.*, pp. 251, 252, note 2.

The equitable principles developed by the French courts, not any specific provisions of the statutes, must be relied upon to safeguard the interests of stockholders and creditors during the period of liquidation. The board of directors continues to exercise its functions notwithstanding the appointment of liquidators.¹ But the courts have held that the functions of the auditors cease as soon as the corporation has entered the period of dissolution.²

Finally, it is to be noted that, although nothing in the bankruptcy provisions of the Commercial Code, or in the special Law of March 4th, 1889, relative to judicial liquidation, compels a corporation to dissolve in the event of insolvency, nevertheless bankruptcy proceedings may often destroy every purpose for which the corporation was created, taking away all its property and leaving it a mere shell. Under such circumstances, the dissolution of the corporation will be decreed upon the request of any party in interest.

2. GERMANY

Existing Law.—The causes for the dissolution of a corporation anticipated by the German Commercial Code are:

1. the limitation of its duration as fixed in the articles;
2. a resolution of the general meeting adopted by a majority of three-quarters of the outstanding capital stock;
3. the initiation of bankruptcy proceedings.³

The Code also speaks of "other grounds" for dissolution without mentioning them specifically. The commen-

¹ Böhm, *op. cit.*, p. 109.

² See cases cited by Lyon-Caen and Renault, *Traité de droit commercial*, ii, p. 909.

³ Comm. C., sec. 292.

tators have interpreted this to refer to causes such as merger (*Fusion*), the abandonment of the *situs* within the state,¹ the amortization of all outstanding capital stock.²

The nullification of a corporation is to be distinguished from its dissolution, although it is expressly provided that, for the purpose of liquidation, the same provisions apply to nullification as to dissolution.³

Except in the case of dissolution on account of bankruptcy, it is the duty of the managers to give notice to the commercial registry that the corporation is about to be dissolved for the specific cause provided by law.⁴ In default of such registration of notice, innocent third parties are not affected by the dissolution.⁵ After the proper basis for dissolution has been established, the corporation exists only for the purpose of liquidation, and is subject to the rules of the Code made specifically applicable thereto. Liquidation in the event of bankruptcy is conducted according to the bankruptcy statute (*Konkursgesetz*).⁶

Liquidation is regularly conducted by the members of the directorate, as liquidators, unless the articles of association, or a resolution of the general meeting, has designated other persons. Stockholders who have held their shares for a period of six months are protected against an unfriendly management. Holders of stock for the period mentioned and representing at least one-twentieth of the capital stock may, for good reasons shown, request the court to appoint liquidators. The court may, under the same conditions, remove liquidators already ap-

¹ Decisions of the Imp. Ct., vii, p. 70.

² Staub, *op. cit.*, i, p. 884.

³ Comm C., sec. 311

⁴ *Ibid.*, sec. 293.

⁵ Staub, *op. cit.*, i, p. 886.

⁶ Comm. C., sec. 294.

pointed and the general meeting may also recall liquidators not appointed by the court.¹

The liquidators must notify the creditors to prove their claims and must reduce the property of the corporation to money.² The amount left over after payment of debts is divided among the stockholders in the usual way, according to the class of the security.³ In carrying out the liquidation, the liquidators are subject to the same control on the part of the supervising council and to the same degree of civil and criminal responsibility as directors of a corporation prior to dissolution.⁴

The distribution among the stockholders may be made only after notice to the creditors to prove their claims has been thrice published in the official newspaper and one year has elapsed thereafter. If a person known to be a creditor has failed to prove his claim, the amount of the claim must be deposited.. If a proven claim is disputed, or if performance of the obligation is impossible at the time, security must be given to the creditor before distribution.⁵

After the liquidation has been completed and final accounting made, it is the duty of the liquidators to give notice to the commercial registry of the discontinuance of the corporate title and to deposit the books and papers of the corporation in a place of security to be designated by the court, there to remain for a period of ten years, accessible to stockholders and creditors by proper authorization from the court.⁶

A sale in bulk of the property of the company is permissible only on resolution of the general meeting by vote of at least three-quarters of the outstanding shares. A sale

¹ Comm. C., sec. 295.

³ *Ibid.*, sec. 300.

⁵ *Ibid.*, sec. 301.

² *Ibid.*, sec. 297.

⁴ *Ibid.*, secs. 298-299.

⁶ *Ibid.*, sec. 302.

in bulk operates as a ground of dissolution even in the absence of other grounds.¹

German law has anticipated the tendency of corporations to consolidate, at least where this is effected by the acquisition by one corporation of the entire property of another. Although the device of the holding company is not expressly provided for by German law, the Code establishes a method by which the entire property of one corporation may be acquired by another without the continued existence of the share capital of both corporations, while at the same time it protects the interests of the shareholders of the corporation whose existence is to be merged. This is accomplished by raising the capital of the vendee corporation without requiring any payment upon the increased capital other than the transfer of the property of the vendor corporation; the consideration for the property passes to the shareholders of the vendor corporation by an exchange of shares, the shares of the vendor corporation being thereupon cancelled and the corporation itself subjected to dissolution.²

Adequate protection is given to the creditors of the vendor corporation in that its property must be kept apart and managed separately until the creditors have been notified of the consolidation and the same provisions made for their benefit as in the ordinary cases of dissolution. The creditors have recourse against the property of the vendor corporation as if there had been no consolidation.³

3. ITALY

Existing Law.—The Italian Commercial Code recognizes the following grounds for the dissolution of commercial associations (including corporations):⁴

¹ Com. C., sec. 303.

² *Ibid.*, sec. 305.

³ *Ibid.*, sec. 306.

⁴ *Codice di commercio*, art. 189.

1. Expiration of the term fixed by the articles.
2. Lack or disappearance of corporate purposes, or the impossibility of attaining them.
3. Accomplishment of the purposes for which the corporation was formed.
4. Adjudication in bankruptcy, even though accompanied by a composition.
5. Loss of the entire capital, or of a considerable part thereof,¹ unless the shareholders agree to make good (*reintegrar*) the loss, or limit the capital to the assets remaining.
6. Consent of the shareholders.
7. Consolidation.

In the event of a consolidation of two corporations, the documents effecting the same must be published in the same manner as the articles of incorporation.² Both companies must publish their final balance sheets according to a uniform plan, and the company to be merged must add a statement of the manner in which it is proposed that the debts shall be paid. The consolidation does not become effective, however, until three months thereafter, unless all the creditors have consented, or all the debts have been paid, or a sum sufficient to cover them has been deposited. During this period, any creditor may oppose the consolidation; its execution is thereupon suspended until opposition is withdrawn or overruled by a judicial decree from which no appeal has been taken.³

¹ Art. 146 provides that if the capital be impaired by one third, the general meeting may decide to dissolve; if impaired by two-thirds, the company must be dissolved unless the capital is replaced or the capital stock reduced to the amount of actual assets.

Ibid., arts. 194, 91, 94, 95.

² *Ibid.*, arts. 195, 196. If there be no opposition during the prescribed period, the consolidation becomes effective and the continuing corporation is subrogated to all the rights and obligations of the merged corporation. Art. 196.

When a corporation is undergoing dissolution,¹ liquidation proceeds according to the provisions of the articles or corporate statutes. The general meeting appoints the liquidators.² After publication of the resolution of the general meeting or decree of the court ordering the dissolution, the directors are prohibited from entering upon any new transaction, under penalty of personal responsibility.³ Actions for and against the company must be conducted by or against the liquidators.⁴ All documents must recite that the company is "in liquidation."⁴ The provisions of law, of the articles, and of the corporate statutes, continue to regulate the affairs of the company wherever consistent with liquidation, and the liquidators are under the same responsibilities as were the directors.⁴

The liquidators must, with the coöperation of the directors, immediately prepare an inventory and balance sheet; they must obtain and preserve the books kept by the directors; they must keep account chronologically of all their transactions relating to liquidation and, upon demand of the shareholders, give information of the condition and progress of the liquidation.⁵

¹ Dissolution begins with the resolution of the general meeting of stockholders, or decree of the court, even though the liquidators have not as yet been appointed. Court of Cassation, Turin, Sept. 23, 1886; *Annali della giurisprudenza*, xx, part i, p. 487.

² *Ibid.*, arts. 197, 210. A quorum of three-quarters of the capital stock is required and an affirmative vote of a majority of the capital stock.

³ *Ibid.*, art. 192.

⁴ *Ibid.*, art. 198. The mandate of the directors ceases with the appointment of the liquidators, but they must coöperate if the latter so require. Art. 211.

⁵ *Ibid.*, art. 200. If the liquidation continues for longer than a year, the liquidators prepare annual balance sheets in the same manner as directors prior to the dissolution. Art. 214.

The directors must render to the liquidators an account of their transactions from the date of the last balance sheet accepted by the shareholders to the beginning of the dissolution; the liquidators may accept or contest the same. If one or more directors become liquidators, this account must be published at the same time as the definitive inventory and balance sheet of the liquidators.¹

When the assets have been liquidated, the liquidators must prepare a final balance sheet indicating the dividend upon each share of stock. This, with the syndics' report, is filed in the office of the commercial court and published; within thirty days, the shareholders may file objections, which must also be published. Two weeks thereafter, all of the objections are submitted to the court, which passes upon them in one judgment; any shareholder may intervene and the judgment, when pronounced, operates *in rem*. If no objection is filed, the balance sheet is deemed approved, and the liquidators are discharged, except in respect of the distribution of assets.²

As in the German law, sums due to stockholders in liquidation but not reclaimed by them are deposited in court, and the books of account of the company are preserved for inspection of interested parties for a period of five years.⁴

4. SPAIN

Existing Law.—There are no provisions of the Spanish Commercial Code especially applicable to the dissolution of

¹ Com. C., art. 213.

² *Ibid.*, art. 215.

³ *Ibid.*, art. 216. The acceptance of the final dividend is also deemed an approval of the accounts and distribution, irrespective of any period to elapse. *Ibid.*

⁴ *Ibid.*, arts. 217, 218. *Seemle*, German Comm. C., secs. 301, 302.

corporations. The Code provides in a general way for the liquidation of commercial associations including corporations. During liquidation, the corporate statutes continue to regulate the activities of the general meeting, which, it is intimated, has control over the progress of the liquidation and power to adopt such resolutions as may be necessary for the common interest.¹

5. SWITZERLAND

Existing Law.—The provisions of the Swiss Code of Obligations² relative to the dissolution of corporations have been taken over from the German Commercial Code with practically little modification, so that it is unnecessary to refer to them at length.

Commentators on the Code of Obligations refer to the corporation as changing its juristic nature by entering into the period of dissolution, so that it no longer remains a corporation in the proper sense of the word, but becomes an association in liquidation in which the several interests of the associates are proportioned to their shares (*Liquidationsverein auf Actien*).³

Comment.—The period of dissolution and liquidation is one which requires extraordinary protection for the interests of both creditor and stockholder. The protection to be afforded to the stockholder ought to be based upon two *desiderata*, somewhat conflicting, yet both of equal importance. On the one hand, it is important that the corporation shall wind up its affairs as nearly in the regular course of business as possible, so as to realize the most for its assets. On the other hand, the corporation should endeavor to discontinue operations at the earliest possible moment, so as not to incur greater loss.

¹ *Código de comercio*, art. 238.

² Arts. 664-670.

³ Schneider and Fick, *op. cit.*, p. 511.

All legislations agree in extending to the stockholders' meeting the right to decide upon a dissolution at any time. German law differs from the French in requiring a three-quarters vote, instead of a bare majority. It is difficult to decide which plan affords greater protection. The necessity of obtaining a three-quarters majority may result in continuing operations for a period beyond that in which the corporation will be able to do so with safety, whereas, on the other hand, a bare majority may be able to take advantage of its power to compel a dissolution to the injury of the minority.

Though the statutory provisions of French law are but fragmentary, the individual shareholder receives ample protection in practice. We have seen that when the general meeting has not been convened by the directors or, having been convened, cannot completely organize itself, any shareholder may petition the court for dissolution. Practice has gone further and has extended a right to the shareholder individually to petition for a dissolution where equitable grounds have been made to appear therefor, irrespective of any statutory provisions.¹ In this the French system approaches the English, and differs from the German. The draft of the German statute of 1884, relating to corporations, also contained a provision giving a single shareholder the right to initiate the proceedings. It was subjected to unfavorable criticism on the ground that it might lead to unfounded petitions for dissolution affecting the credit of solvent corporations. It was therefore eliminated from the draft.²

¹ Lyon-Caen and Renault, *Traité de droit commercial*, i, 906, *bis*; Vavasseur, *Traité des sociétés civiles et commerciales* (5th ed.), ii, p. 915.

² Böhm, *op. cit.*, p. 106, citing *Motive* to the draft of this law. Berlin, 1883, pp. 366-367.

CHAPTER IX

LEGISLATION AND REFORM IN ENGLAND AND AMERICA.— DISSOLUTION

THE management of corporations under all the systems with which we are concerned is confided either to a board of directors acting through officers or through a committee, or else to a directorate in conjunction with a supervising council, as in Germany and Italy. While the corporation is a going concern, the discretion in all matters appertaining to its management must be left to its operating organs, subject to such restrictions as are necessary to insure to creditors and stockholders honest management of its affairs and a just distribution of its profits. Government, at least under our present system, does not assume to interfere with the freedom of either individuals or corporations in the conduct of business, so long as they act lawfully and meet their obligations. Once it is determined, however, either by the will of the members, or by court decree, that a corporation shall be wound up, its character as a free organism ceases. The rights and liabilities of all interested parties may be deemed fixed, even though not definitely ascertained; and the estate of the corporation becomes a trust to be administered in such manner and for such purposes as the law may determine.

This ideal has been most completely realized by English legislation. "Winding up" may be either (1) by the court, or (2) voluntary, or (3) subject to the supervision of the court. A company may be wound up by the court on

certain contingencies set out in the statute, the important ones being: (a) when the court thinks it just and equitable, (b) when the company is unable to pay its debts, and (c) when the company, by special resolution, resolves to be wound up by the court.¹ Application for winding up may be made by any contributor (*i. e.* any person liable to contribute to the assets of the company in the event of its being wound up), or creditor, or any prospective or contingent creditor, or by the company. The court has full power to grant or refuse the petition for winding up. Upon granting the order, all actions against the company are stayed, except those continued by leave of the court.² At the time of the winding-up order, a report of the condition of the company's affairs must be made to a person connected with the bankruptcy court who is styled the "official receiver." The court has power to appoint one or more persons called "liquidators" to carry out the winding-up order, the official receiver being usually appointed to serve only until (or pending) a winding-up order, the court (after an order is issued) afterwards appointing a liquidator. The liquidator (unless he be the official receiver) must give security to the satisfaction of the board of trade, which, in England, is an official body.³ As soon as practicable, he must make a report of the condition of the company, stating whether it has failed and the cause thereof, and whether in his opinion further investigation as to the formation and conduct of the business is necessary. The liquidator takes into his custody and control all the property and things in action to which the company appears entitled.⁴ He has power, with the consent

¹ Companies Act, 1908, secs. 122, 129.

² *Ibid.*, sec. 142.

³ *Ibid.*, secs. 146, 147, 149, 153, 154.

⁴ *Ibid.*, sec. 150.

of the court, to bring or defend any action or other legal proceeding, to carry on the business of the company, and to employ a solicitor or other agent to assist him.¹

A committee of inspection is chosen from the creditors and contributories. This committee meets from time to time and may act by a majority of its members, and, subject to the provisions of the law, the liquidator shall have regard to its directions in the administration of the assets of the company.²

All sums received by the liquidator must be deposited by him, at such times as the board of trade shall direct, to the "companies liquidation account" at the Bank of England, unless the committee of inspection shall satisfy the board of trade that an account with another bank is desirable. The liquidator must, at least twice a year, make a report in usual form and send it to the board of trade for audit. The board of trade is given supervisory power over the liquidator, his books and vouchers.³

As soon as the winding-up order is made, the court settles a list of contributories. Every present member is liable to contribute to the assets of the company, but not in excess of unpaid subscriptions; and all past members for the year preceding are liable to contribute for the payment of all debts contracted while they were members, but not in excess of unpaid subscriptions, and not unless it is proved to the court that the existing members are unable to pay the contributions required of them.⁴

A voluntary winding up may be had when the period fixed by the articles of the company for its duration has ex-

¹ Companies Act, 1908, sec. 151.

² *Ibid.*, secs. 158, 160.

³ *Ibid.*, secs. 155, 159.

⁴ *Ibid.*, sec. 123.

pired, or an event fixed as the limit of its duration has occurred, and the company, by special resolution, resolves that it shall be wound up.¹ As in Continental European countries, the winding-up period is deemed to begin from the time of passing the resolution.² Generally speaking, the only difference between the voluntary and judicial winding up is that the appointment of liquidators is made by the company in general meeting instead of by the court. The liquidator appointed by the company in voluntary winding up has the same rights and duties as if appointed by the court.

The court may at any time make an order that the voluntary winding up shall continue, but subject to the supervision of the court, and with liberty to contributories, creditors and others to apply to the court to exercise its supervisory functions.³ Where the court assumes supervision, the liquidator has the same rights and duties as if the court had not stepped in, except that the court may remove him. In general, this third method of winding up is similar to the first, except that certain designated sections of the Companies Act do not apply.⁴

The great value of the English statute, as far as it relates to the dissolution of corporations, lies in its completeness. It creates an uniformity in the method of liquidation that makes for efficiency and economy. At the same time it gives a wide amount of control over the progress of liquidation

¹ Companies Act, 1908, sec. 182.

² *Ibid.*, sec. 183.

³ *Ibid.*, sec. 199.

⁴ *Ibid.*, sec. 203. In preparing this resumé of the provisions of the English act referring to the winding up of companies, the author has had the use of MS. prepared by Dr. William Draper Lewis and his assistants R. C. Heisler and H. Shapiro, on behalf of the Legislative Drafting Association, and submitted to the Commissioners of Uniform State Laws.

to the persons most interested in safeguarding the assets, namely, the creditors and the particular stockholders liable for contribution.

In the United States, dissolution is effected by various methods, according to whether it results from the operation of state insolvency statutes, or from proceedings in equity, or from some voluntary act of dissolution. The Federal Bankruptcy Act does not provide for the dissolution of insolvent corporations. The state statutes are seldom complete; provisions relative to the various methods and causes for dissolution must be sought for in separate statutes and in the practice of the courts of equity.

In California, a corporation may be dissolved by the court on voluntary application, as evidenced by the resolution of two-thirds of the members, or of the holders of two-thirds of the capital stock. In this proceeding, the directors or managers of the affairs of the corporation are considered to be trustees of the creditors and stockholders, and have full power to settle its affairs.¹ The corporation may also be dissolved at the instance of any creditor in the event that it lose or dispose of all its property and fail for a period of two years to elect officers and transact business.²

In Illinois, courts of equity are given power to dissolve or close up the business of any corporation in the event of insolvency or in the event that the corporation shall allow any execution to be returned unsatisfied and remain thus for not less than ten days. Suits in equity may thereupon be brought against all persons who were stockholders, to

¹ Cal. Code Civ. Pro., sec. 1228; by amendment approved March 16th, 1907, all claims and demands against the corporation must be satisfied and discharged before the application is made. So in Wash., Ballinger's C., sec. 4275; and in Mont., Code Civ. Pro., sec. 7324.

² Cal. Civ. C., sec. 358,

the extent of unpaid subscriptions, but only after exhausting the assets of the corporation.¹

In New Jersey, a voluntary dissolution must be voted first by a majority of the whole board of directors and thereafter by a vote of two-thirds in interest of all stockholders. The court has full power to continue the directors as trustees or to appoint one or more persons to be receivers of the corporation and conduct the winding up; this applies both to voluntary and involuntary proceedings.²

Under New York law, a corporation may be dissolved involuntarily, at the suit of the attorney-general, if its capital stock be not paid up within the time prescribed, or in the event of abandonment of the use of its franchise.³ It may also be dissolved by action, either at the suit of the attorney-general, or, in default thereof, by a creditor or stockholder, after obtaining leave of the court. The grounds of such action must either be that the corporation has remained insolvent for one year; that it has neglected or refused for at least one year to pay or discharge its notes or other evidences of debt; or that it has suspended its ordinary and lawful business for at least one year.⁴ The court appoints one or more receivers for the purpose of winding up. In addition to these proceedings, directors, trustees,

¹ Ill. Gen. Corp. Law, sec. 25. In Minnesota, stockholders of all except manufacturing corporations are liable for its debts to the amount of stock held by them in addition to the amount originally paid in. See Kuhn in *Yale Law Journal*, April, 1908, p. 457.

² N. J. Corp. Act, sec. 56. *Seemle*, Del. Gen. Corp. L. 1899, sec. 39.

³ N. Y. Business Corp. L., sec. 5.

⁴ N. Y. General Corp. L., secs. 101, 102. *Seemle*, Wis. Sanborn's Stats. sec. 1763. In Minnesota, stockholders owning not less than 40 per cent. of the capital stock may pray for dissolution, if the corporation has continued in business for at least three years, during which it has sustained losses impairing the capital stock to the extent of 25 per cent. Rev. L. 1905, sec. 3175.

or other officers must present a petition to the Supreme Court for voluntary dissolution whenever directed so to do by a majority in interest of the stockholders. The court may entertain or dismiss the application, and the proceedings are conducted in the usual way, through appointment of a receiver and the exercise of the ancillary powers of a court of equity.

It is noticeable in all this legislation that very little official coöperation is sought from or permitted to the creditors and stockholders themselves. The management of the corporation at its most critical period is thus left in the hands of the court, which, of necessity, must act through its receiver. This involves great expense and the waste of corporate assets in a routine procedure. Furthermore, the system has made it customary if not absolutely essential to appoint as receivers members of the legal profession or other persons familiar with the legal machinery incident to receivership, but frequently ill-fitted to engage in business transactions requiring business rather than legal judgment. The assets of a corporation in liquidation, therefore, are sacrificed to the demand for immediate liquidation. This is neither the fault of the courts nor of lawyers, but is ascribable to the lack of constructive legislation conducive to a business administration of the affairs of corporations during the dissolution period.

The Federal Incorporation Bill does not provide any comprehensive system for the dissolution of corporations to be formed under it. If shareholders owning two-thirds of the stock determine to dissolve, the board of directors must give notice to creditors to present their claims. By implication of the statute, the directors then proceed to liquidate.¹ The bill also proposes a reform of consid-

¹ Senate Bill, no. 6186, 61st Cong. 2nd Sess., sec. 29.

erable novelty as applied to industrial corporations, taken from the federal statutes in respect of national banks. Whenever a corporation shall have failed to pay off any of its written obligations, or has permitted an execution to be returned unsatisfied, the commissioner of corporations may appoint a special agent who shall ascertain whether or not the corporation is in an unsound financial condition. If the commissioner is satisfied that the corporation is either insolvent, or of such unsound financial condition as to make its continuance in business contrary to the public welfare, he may appoint a receiver, who shall become entitled to possession of all the real and personal property of the corporation, and have all the powers of a receiver appointed by a court of equity.¹

The notable feature of present-day demands for reform is the emphasis laid upon the necessity for supervision by an administrative body, rather than by a court. The nature, importance and complexity of modern business requires that the affairs of corporations in the dissolution period be conserved by bodies assuming special functions. The American constitutional system as developed over a period of little more than a century has already concentrated many quasi-administrative duties into the hands of courts. If functions connected with ordinary business administration are to be added, the orderly procedure of regular judicial business will suffer, while corporations will be dissolved under a routine or conventional system, administered without regard to the requirements of sound business and finance. This will be productive of sacrifice rather than conservation. The English law presents a plan both practical and safe, to which American legislatures should give earnest consideration.

¹ *Loc. cit.*, sec. 31.

INDEX

- Abuse of corporate forms, 66, 99
- Actio doli*, 21
- Action sociale*, 119
- Action individuelle*, 119
- Administrateurs*, 116
- Administradores*, 139
- African Company, 52
- Agent, authorized, 124, 141
- Aktiengesellschaften*, 68, 93
- Alabama, 108
- Allotment of shares, 106, 107
- Amendment of articles, 84, 137
- America, 97, 144, 166;
 see individual states
- America, discovery of, 48
- American law and English, 111, 133
- Amortization, 93, 119, 123, 125, 142, 158
- Annual balance sheet, 128;
 see Balance Sheet
- Annual meeting, 52;
 see General Meeting
- Annulment of unpaid shares, 92
- Apporteurs*, 58, 59, 62, 95
- Apports*, 59, 64, 111
- Articles, amendment of, 84, 137
- Articles of association, 70, 91, 104
- Assada merchants, 50
- Assemblée Générale*, 116
- "Assistants," 52, 53
- Associations, commercial, 91
- Associations, limited liability, 67
- Atto costitutivo*, 88
- Attorney-general, 109, 171
- Auctor emptio*, 23
- Auditors, 73, 74, 117-119, 121, 144
- Auditors appointed by court, 129
- Auditors, duties of, 130, 138, 145
- Aufsichtsrath*, 70
- Authorities, list of, 9
- Austria, 65, 66
- Baden, 65
- Balance Sheet, 128, 138, 139, 140, 142, 144, 145, 162, 163
- Bank of England, 53, 54, 168
- Bankers and brokers, 76, 77, 85;
 see Stock Exchange
- Bankruptcy, 133, 157, 161, 170
- Banks in Spain, 91
- Bavaria, 66
- Bibliography, 9
- Board of management, 140;
 see Directors' Council
- Board, proportional representation in, 148
- Bolivia, 90
- Bonds as guarantee, 137
- Borough a corporation, 43
- Bremen, 66
- Bruce, 49
- Bruges, 45
- Bubble Act, 55, 97, 101
- Building associations, 91
- Bulletin, official, 89
- Burgess, Prof., 13, 106, 148
- Calais, markets at, 45
- California, 153, 170
- Capital, amount paid within year, 95, 103, 108
- Capital, authorized, 82
- Capital, loss of, 119, 161
- Capital, reduction of, 123, 152
- Capitalization, 103
- Centralization of industry, 100
- Certificate of incorporation, 102, 103, 105
- Charles I, 50, 52
- Charles II, 51
- Charter of Elizabeth, 49
- Charter from Crown, 97
- Charter from Parliament, 51, 53, 55, 99
- Cives*, 19
- Civil War, 113
- Classification of corporations, 15
- Code, Civil, 67, 93, 117, 119
- Code de commerce*, 56, 65, 66, 85, 90
- Code, German, 122, 160
- Code of Obligations, 93, 143, 164
- Code of 1829 (Spain), 90
- Code of 1886 (Spain), 90

- Codes of Spain, 90, 91
Codice Albertino, 86
Codice d' Italia, 86
Codigo de commercio, 90
 Coke on Guild Merchant, 43
Collegia, 18, 21
 Columbus, 90
 Commerce, tribunal of, 156
 Commercial associations, 91
 Commercial Code, 66, 67, 73, 79, 116, 128, 157
 Commercial court, 87, 136
 Commercial registry, 130
Commissaires, 116
 Commission, Industrial, 146
 Commissioner of Corporations, 114, 147
 Commissioners of Uniform Laws, 103, 108, 147, 149, 152
Communitas, 43
 Community in Italy, 20
Companias anonimas, 91
Companias mercantiles, 91
 Companies act as bankers for government, 53
 Companies Act (Eng.), 98, 99, 104, 169
 Companies, guaranty, 101
 Companies, holding, 149, 150
 Companies, joint-stock, 46 *et seq*
 Companies, officers of, 52, 53, 54
 Companies regarded as partnerships, 54
 Companies, regulated, 45, 46
 Companies, share, 101
 Companies, unchartered, 54
 Company, limited, 98
 Company of staple, 44
 Company, unlimited, 98
 Concessionary system, 98
 Conference of Nuremberg, 66
 Connecticut passes first general act, 99
 Consolidation, 51, 99, 137, 160, 161
Constitutio personalis, 66
 Continental systems, 60, 61
 Contributions in kind, 93
 Control, direct, 144
 Control, indirect, 145
Controlstelle, 141
 Copper Mines in England, 52
 Costa Rica, 90
 Corporate title, 101
 Corporate types in Ancient times, 17
 Corporate types in Middle Ages, 30
 Corporation authorized to do business, 72
 Corporations, classification of, 15
 Corporations, commissioner of, 114, 147
 Corporations, consolidation of, 99, 160, 161
 Corporations, dangerous, 81
 Corporation, definition of, 13
 Corporation, designation of, 102
 Corporations, encouragement of, 150
 Corporations, government and, 166
 Corporations, operation of, 116-140
 Corporations, organization of, 56-93
 Corporations, name of, 102
 Corporations Congress, 121
 Corporations, defect of French, 121
 Corporations, dissolution of, 155, 164
 Corporations, industrial, 145
 Corporations in England, 43
 Corporations in France, 56
 Corporations, taxation of, in U. S., 100
 Corporations, theory of, 20
 Corpus, 21
 Council and liquidators, 159;
 see Liquidators
 Council, designated, 72, 73
 Council responsible to corporation, 128
 Council, supervising, 74, 126, 127, 140
 Courts and dissolution, 157;
 see Dissolution
 Courts and organization, 83;
 see Organization
 Courts, commercial, 87, 136
 Courts in Switzerland, 95
 Courts, mandate of German, 133
 Courts, mild in France, 130
 Courts, powers of, 136, 166, 167
 Courts, powers of German, 84
 Courts, severe, 130
 Craft guilds, 44
 Creditors, not protected, 107
 Creditors, protection of, 56-93, 116-140, 155-164
 Criminal code, 80
 Criminal penalties, 79, 89, 133, 139, 143, 152
 Crisis, 109
 Cromwell, 50, 51
 Cumulative voting, 149
 Curia, 21
Decharge, 78
 Declaration of organizers, 73, 74
Decuriones, 21
 Definitions, obscurity of, 14
 Delaware, 107, 111
 Directorate, 72, 73, 74, 94, 123, 124
 Directorate and council, 126, 127
 Directors allot stock, 106, 111
 Directors and liquidators, 157

- Directors, breach of duty of, 125
 Directors, direct liability of, 151
 Directors, duties of, 56, 126, 135, 146
 Directors, election of, 149
 Directors, election of, for more than year, 141
 Directors liable, 114, 115, 117, 118, 151
 Directors may not delegate functions, 126
 Directors may not proxy, 135
 Directors must give entire time, 125
 Directors named in by-laws, 104, 105
 Directors not named, 104
 Directors pay on shares, 107
 Directors, rights of individual, 135, 136
Direktion, 141
 Discovery of America, 48
 Dissolution, 108, 119, 137, 145, 164
 Dissolution in Continental Europe, 155-164
 Dissolution in England, 166
 Dissolution in U. S., 170
 Dissolution, voluntary, 172
 Dividends, unearned, 153
Dol, 117
 Draft act, 108, 147
 Dutch companies, 56
 Dutch East India Company, 49
 East India Company, 48, 53
 East India Company, joint-stock principle, 48
 East Indies, voyages to, 48
 Eastland company, 46
 Edward III, guilds under, 44
 Elizabeth, 48
 Elizabeth, charter of, 49
 Embezzlement in California, 153
 Enforcement of corporation law in France, 61-63
 England, 43, 97, 110, 111, 144, 166
 Expansion, colonial, 113
 Expiration of articles, 155, 161
 Extension, 137
 Factories, 49
 False statement, 79, 80, 114, 145, 153
Fautes, 117
 Federal incorporation, 13, 109, 113, 115, 147, 151
 Federal Incorporation Bill, 151, 172
 Filing of annual report, 106
 Financial company, first, 55
Fiscus, 19
 Flanders and Henry IV, 45
 France, corporations in, 56 *et seq.*, 116, 155
 Franchise in Rome, 22
 Franco-Prussian War, 80
 French Code, 56, 82, 83, 85, 90
 French Law of 1867, 57, 59, 63
Fusion, 158
Gaceta, 140
 General corporation laws, 99
 General meeting, 119, 126, 128, 129, 130, 136, 140, 141, 144, 155, 165
 General Society of Traders, 51
Generatversammlung, 123
 Georgia, 107
Gerentes, 140
 German attitude, 85, 133
 German Commercial Code, 66, 67, 89, 133
 Germany, 65, 122, 157
Gewerkschaften, 52
 Gierke quoted, 14, 82
Gilda mercatoria, 43
 Gray on definition of corporation, 14, 15
 Greek city-state, 17, 19
 Group forms in ancient times, 17
 Group forms in middle ages, 30
Gründer, 71
 Guaranties, German, 133, 134
 Guild merchant, 43, 44
 Guilds, craft, 44
 Hamburg, 66
Handelsgesetzbuch, 68
 Hanse towns, 45
 Henry I, 44
 Hesse, 65
 Holding companies, 149, 150
 Hudson Bay Company, 52
 Ihering, 81, 85, 108, 133
 Illinois, 149, 170
 Imperial period, 22
 Imprisonment, 79, 130, 131;
 see Criminal Penalties
 Incorporation, federal, 113, 115, 147, 151
 Indemnity to France, 80, 81
 Industrial commission, 146
 Introduction, 13
 Iowa, 112, 115
 Ireland, staples in, 45
 Italian Code, 86, 89, 138, 139
 Italy, 20, 85, 94, 134, 139, 160
 Italy, cities of, 20
 James I, 50, 52
 Joint stock companies, domestic, 52
 Joint stock, confusion in, 50
 Joint stock in Dutch Company, 49, 50
 Joint stock principle, 48

- Judicial control, 95
- Junta Generale*, 92
- Kansas, 149
- Konkursgesetz*, 158
- Land, exploitation of, 49
- Latin-American, states, 90
- Law of 1844 (England), 97
- Law of 1855 (England), 98
- Law of 1862 (England), 98
- Law of 1867 (France), 57, 59, 63, 116, 118, 120, 155, 156
- Law of 1884 (German), 67, 78, 165
- Law of 1889, 157
- Law of 1893 in France, 65
- Law of 1900 (England), 98, 99
- Legislation, social, 132
- Legislative development in America, 99
- Legislative development in Germany, 65
- Legislative development in Switzerland, 93
- Legislative Drafting Association, 5
- Levant Company, 48
- Liability, 119;
 - see Shareholders, Directors
- Liability, limited, 66, 98
- Liability of bankers, 76, 77
- Liability of organizers, 75, 76
- Liberal laws, 100
- Limitation of par value, 103, 104
- Limitation of powers, 125
- Limitations, maximum, 109
- "Limited," 101
- Limited companies, 57
- Limited liability, 66, 98
- Limited Liability Act, 98
- Liquidation, 156, 157, 159, 163, 164, 165, 168
- Liquidators, 130, 131, 133, 162, 167
- Liquidators notify creditors, 159
- Liquidators, removal of, 158, 159
- Majority rule, 148
- Managers, 64, 94, 124, 140, 149;
 - see Directors
- Management, double organ, 120
- Management, single board, 120
- Managing committee, 141
- Manceps*, 23
- Mancini, 86
- Mandamus, 145
- Mandataries, 116, 117
- Meeting, annual, 121;
 - see Meeting, General
- Meeting, General, 116, 117, 118, 119, 123, 126, 128, 129, 130, 136, 140, 141, 144, 155, 165
- Memorandum, 102, 103, 104
- Merchant adventurers, 45, 46
- Michigan, 107, 108, 149
- Middle Ages, ideas of, 14
- Minimal requisites, 70
- Minimum subscription, 110
- Minority stockholders, 88, 137, 148
- Misrepresentation, 130;
 - see False Statement
- Missouri, 149
- Municipality, 21
- Municipium*, 19
- Napoleonic Code, 56, 65
- Nebraska, 140
- New Jersey, 107, 171
- New York, 107, 115, 171
- Nominative shares, 70, 80
- North German Confederation, 66
- Nullification, 84, 108, 158
- Nullity of corporation, 61, 64, 65, 84
- Nuremberg, conference at, 66
- Officers of companies, 52, 53, 54
- Ohio, 149
- Operation in Continental Europe, 116-142
- Operation in England and America, 144-153
- Organization, 56-115, 142
- Organization in England and America, 97-116
- Organization, simultaneous, 72, 86
- Organization, successive, 72, 86
- Organization, tripartite, 133
- Organizers, 71, 72, 73, 95, 111
- Organizers, liability of, 64, 65, 75, 76, 79, 88, 90
- Origin of corporations in England, 43-55
- Overcapitalization, 107, 109, 113, 115, 137
- Overspeculation, 57
- Panic, 109
- Palatinate, 65
- Paris, liquidators in, 156
- Partnerships, 57, 66, 97
- Penal Code, 63, 122
- Penalties,
 - see Criminal Penalties
- Pennsylvania, 107
- Permanency of dividends, 128
- Persons in Switzerland, 93
- Populus*, 18, 21
- Posen, 65
- Preferential voting, 71
- Preferred stock, 70

- Projet*, 86
Prokuristen, 124, 141
 Promoters, 62, 108, 111
 Property in Egypt, 22
 Property in Greece, 17, 18, 22
 Property in Rome, 19, 22
 Property, overvaluation of, 62
 Property, purchase of, 71, 114
 Property, purchase of shares by, 61, 62, 84, 114
 Property, sale of, 114, 159
 Property, social, 19, 22
 Property, state, 19
 Prospectus, 110, 111, 114, 119, 153
 Protection of creditors, 56-93, 116-140, 155-164
 Prussia regulates corporations, 65
 Publicity, 81, 104, 110, 114, 115, 119, 121, 128, 144-147, 156
 Punishment, 133, 139, 143, 152;
 see Criminal Penalties
 "Qualified" organization, 71
 Railroads, 65, 91
 Rates, and the courts, 84
 Recall by meeting, 123
 Reduction of capital, 152
 Registered shares, 69, 70
 Registration, 74, 75, 82, 91, 98, 104, 110
 Registration of agent, 124
 "Regulated" companies, 45, 46
 "Regulations," 104
 Report for private purposes, 147
 Report for public purposes, 147
 Report of auditors, 145
 Reports, annual, 106, 138, 144, 147
 Reports, false, 153;
 see False Statement
 Reports, special, 147
 Representation, proportional, compulsory, 148, 149
 Representative, 124, 141
 Republican period, 20
 Reserves, 119, 129, 143
Res publicae, 19
 Revenues from corporations, 100
Revisoren, 73, 74
 Revisors, duties of, 138
 Revolution, 99
 Rhode Island, 112
 Right to do business outside state, 100
 Rome, corporations in, 43
 Rome, property in, 18
 Rule of majority, 148
 Sardinia, 86
 Savigny, 19
 Saxony, 66
 Seal of borough, 43
 Separate entity, 20, 21
 Separation of persons, 20
 Shareholders, consent of, 124
 Shareholders elect officers, 52
 Shareholders, few, 107
 Shareholders, liability of, 53, 85, 97, 99, 103, 110, 122, 131, 168
 Shareholders, list of, 146
 Shareholders, loan to, 152
 Shareholders, meeting of,
 see General Meeting
 Shareholders, minority, 78, 129, 141, 148
 Shareholders, protection of, 56-93, 116-140, 155-164
 Shareholders, rights of, 53, 112, 140
 Share capital, 103
 Share certificates, 137
 Share warrants, 98
 Shares, bearer, 69, 70, 92, 98
 Shares issued, 52, 75
 Shares, nominative, 70, 80
 Shares, number of, 103
 Shares, par value, 69
 Shares, registered, 69, 70
 Shares, transfer, 94, 97, 112
 Simultaneous organization, 86, 87
Simultangruendung, 72
Sindaci, 137, 138
 Situs of company, 87, 158
Società anonima, 86
Societas, 23
Société en commandite, 56
Sociétés anonymes, 56, 93
 Society of Mines, 52
Socii, 23
Sodalitas, 18
 Sohm quoted, 18
Souscription integrale, 61
 South Carolina, 108, 149
 South Sea Company, 54, 55;
 see Bubble
 Spain, 90, 94, 139, 163
 Spanish codes, 90, 91, 95
 Spanish invasion, 46
 Spanish law, 90, 91
 Special Act, 99
 Speculation discouraged, 69
 Staples, 44, 45, 46
 State, business outside, 100
 State, sovereignty of, 18
 Statement, 79, 80, 114, 145, 146;
 see Report, False statement

Statuten, 70
 Stock, amount of, 102
 Stock, appraisers of, 112, 113
 Stock, common, 70
 Stock, decrease of, 137
 Stock exchange, 132, 138
 Stock for property, 61, 62
 Stock, increase of, 137
 Stock, payment of, 107
 Stock, preferred, 70
 Stock, rule of issue of, 87
 Stock watering, 79
 Stockholders,
 see Shareholders
 Stocks not to be listed, 79
 Subscription, 72, 87, 106, 107, 110
 Subscriptions repaid, 90
 Successive organization, 72, 87
Successivgründung, 72
 Supervisors, 126, 176
 Swiss code, 87, 88, 95, 140
 Switzerland, 93, 140, 164
 Syndics, 135-138
Tantiemes, 126
 Thaller, 65
 Third parties, 125
 Thomas A. Becket, 45
 Title, corporate, 101

Tribunal of commerce, 156
Truffa, 136
 Trustees, 146;
 see Directors
 Tudors, the, 47
 Turkey Company, 46, 47, 48
 Uniform Laws, 103, 108
 Uniform State Laws, Commissioners of,
 147, 149, 151
 Unincorporated companies, 97, 101
 United Company of Merchants, 51
 Verification, 82, 83, 84, 87, 88
Verwaltung, 94
Vorstand, 70, 72, 123
 Voting by proxy, 149
 Voting, cumulative, 149
 Voting of shares, 71, 131, 132
 Voting, proportional, 71
 Westphalia, 65
 William and Mary, 54
 Wilson, Woodrow, 17
 Winding up, 166, 167, 168
 Winding up, judicial, 168, 169
 Winding up, voluntary, 168, 169
 Wisconsin, 108
 Wurtemberg draft of 1839, 66
Zeichner, 94
Zeichnungsschein, 72

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